



NEPAL
ECONOMIC
FORUM

nefport

DOING BUSINESS IN FEDERATED NEPAL

DOCKING NEPAL'S ECONOMIC ANALYSIS

ISSUE 32 | MARCH 2018

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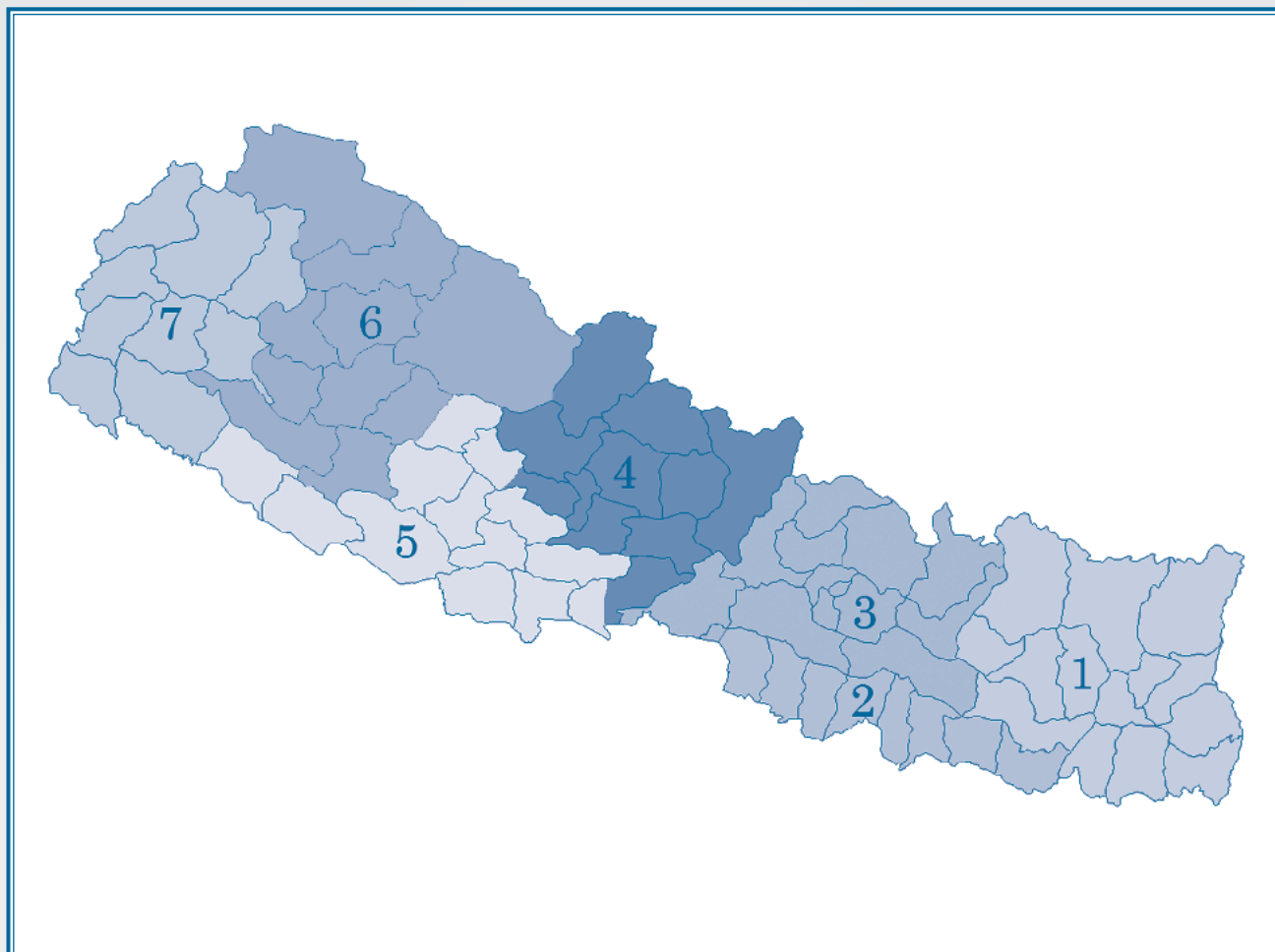
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NEPAL FACTSHEET



KEY ECONOMIC INDICATORS

GDP	USD 23.31 billion	GDP Growth rate (%)	6.9%
Rank	105	Inflation (annual %)	3.2%
GNI per capita (Atlas)	USD 730	Agricultural growth rate (annual %)	5.3%
Rank	196	Industrial growth rate (annual %)	11.0%
GNI (PPP)	USD 2,520	Service Sector growth rate (annual %)	6.9%
Rank	187		
Gross Capital Formation (% of GDP)	28%		
HDI	0.558		
Rank	144		

Sources:

Left Table – Statistics time; The World Bank; HDI figure from Human Development Reports of the UNDP;

Right Table - Budget 2017/18- Ministry of Finance, May 2017



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The word 'province/provincial' and 'state' has been used interchangeably.

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EDITORIAL

This quarter has been a historic one for Nepal. Following years of transient governments, we finally have a government in place that has been sworn in for five years and will hopefully serve their entire tenure. As such, this quarter marks the end of the political transition that began in April 2006.

The people of Nepal have high expectations for the new government. Some positive developments have added to the optimism. A seasoned technocrat, Dr. Yuvraj Khatiwada, has been appointed Finance Minister. Dr. Khatiwada brings in experience from being the Vice Chairman of National Planning Commission (NPC) and the Governor of Nepal Rastra Bank (NRB). Apart from that, he also brings in international exposure and experience that can benefit Nepal.

In the last quarter, NEF has been engaged in the discourse on doing business in federated Nepal. We have conducted research and held several discussion sessions on the topic where we have collected opinions from key stakeholders in different fields. Discussions have converged on what the new federated structure means to Nepal's business and economy. We therefore dedicate this issue to the work that has been done on the topic and is continuing to be done.

NEF continues to strive to be a repository of analysis on how Nepal will take shape as an investment destination and how the Nepali economic development paradigm will shape up in the days to come. As Secretariat to the Himalayan Consensus Summit, NEF is preparing to host the third summit from 23–25 March 2018. In keeping with NEF's aim to work on regional platforms, a Himalayan Consensus Think Tank Consortium was successfully held in Delhi in January of this year. The Consortium will further crystallize in the upcoming summit.

NEF was once again featured in the Go to Think Tank list in 2017. We continue to be overwhelmed with the support we receive from various quarters to keep the humble work going.

This edition is a Doing Business in Federated Nepal special, highlighting the forthcoming challenges and opportunities. We would like to thank all the key contributors especially Mr. Rajeev Malhotra (Professor and Executive Director at Center for Development and Finance, Jindal School of Government and Public Policy, India), Mr. PB Jayasundara (Senior Economist and Former Secretary, Sri Lanka) and Mr. Jeffrey C. Fine (International Consultant, Canada) for helping us make this issue an enriching one.

We continue to look forward to your valuable comments and suggestions.

Sujeev Shakya
Chair, Nepal Economic Forum



GENERAL
OVERVIEW

POLITICAL OVERVIEW

Elections for the House of Representatives (HoR) were held in two phases on November 26 and December 7, 2017 and the election for the National Assembly (NA) was held on February 7, 2018, thus forming a bicameral legislature system in Nepal. The left alliance secured a majority in both the houses and state assembly meetings were held for the first time. Additionally, Chief of State, Chief Ministers and temporary state capitals were declared.

Federal Parliament of Nepal: The Constitution of Nepal has instated a bicameral federal legislature system in Nepal comprising of the HoR and the NA. Elections for the members of HoR were held in two phases on November 26 and December 7, 2017 and the election for the NA was held on February 7, 2018.

House of Representatives elections:

The HoR elections were held for a total of 275 members, 165 of whom

were elected through the first past the post (FPTP) electoral system with one member being elected from each election constituency. The remaining 110 members were elected via the proportional representation (PR) electoral system where voters voted for political parties and the whole country was considered as a single electoral constituency.

The results of the HoR elections were as follows:

The elections resulted in a victory for the left alliance, where a total of 174 seats were obtained by the left alliance in the HoR, also referred to as the lower house of the federal parliament.

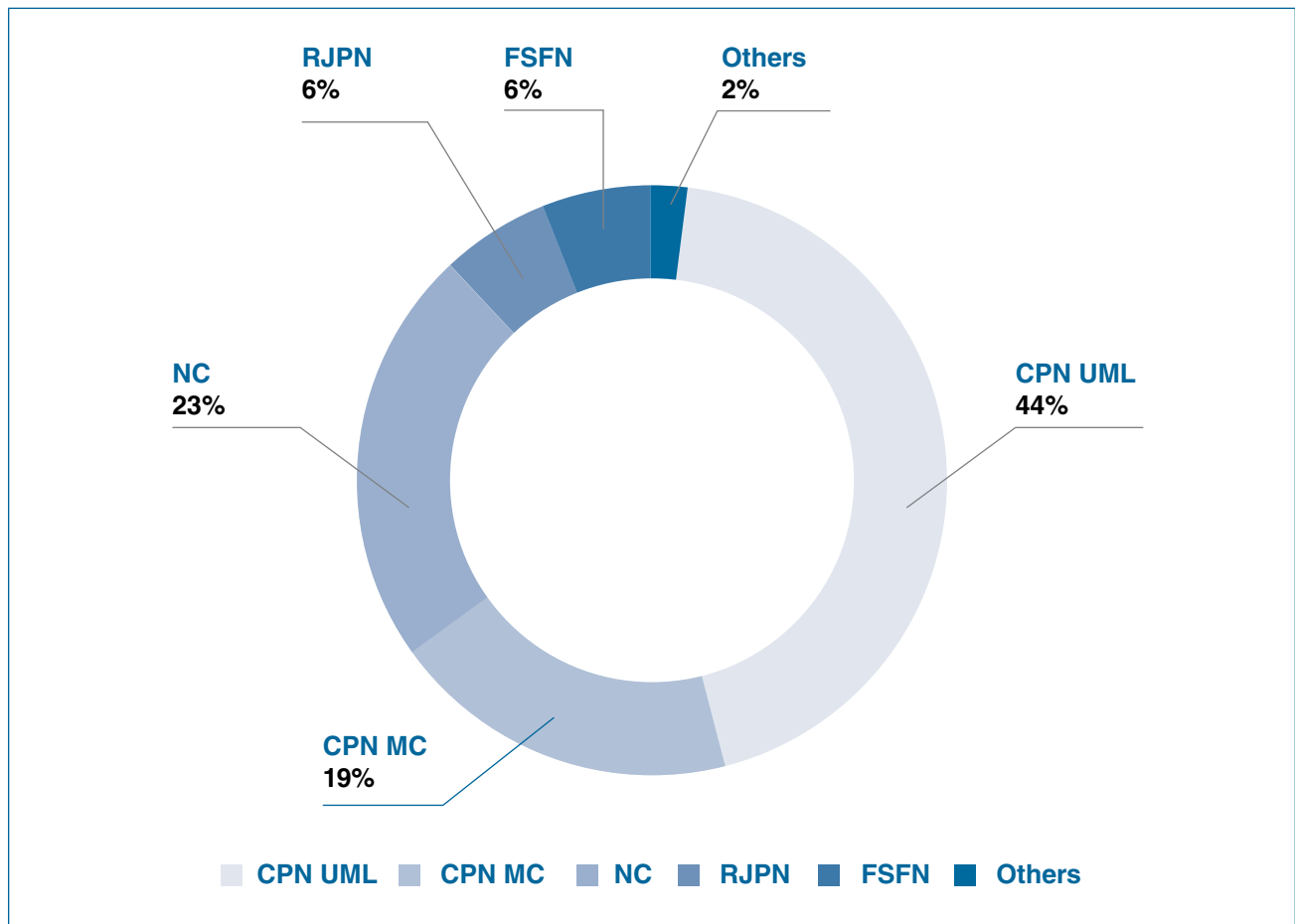
National Assembly elections:

In the NA, also referred to as the upper house of the federal parliament, 24 out of a total of 59 members were elected undisputedly and 32 members were elected under the single transferable electoral system by an

Table 1: Results from House of Representative elections

Parties	FPTP Seats	PR Seats	Total Seats
CPN UML	80	41	121
CPN MC	36	17	53
NC	23	40	63
RJPN	10	6	16
FSFN	11	6	17
Others	5	0	5
Total	165	110	275

Source: Election Commission Nepal

Figure 1: Composition of House of Representatives

electoral college that was comprised of a total of 1,669 out of 1,677 voters. The Electoral College was comprised of 1,234 mayors and deputy mayors of municipalities, along with the chairpersons and vice-chairpersons of the rural municipalities, and 443 members from the State Assemblies.¹

Under the constitutional provision, three members of the NA were nominated by President Bidhya Devi Bhandari upon the recommendation of the Government of Nepal. The left alliance secured a two third majority in the NA. The results of NA elections are as follows:

State elections: The state elections in Nepal were held alongside the parliamentary elections in two phases on November 26 and December 7, 2017 with the left alliance achieving a majority in six of the states whereas in State 2, the Federal Socialist Forum Nepal (FSFN) obtained a majority of

Table 2: Members of the National Assembly

Parties	Elected Seats	Nominated by the President	Total Seats
CPN MC	12	3	59
CPN UML	27		
NC	13		
RJPN	2		
FSFN	2		
Total	56		

Source: Election Commission Nepal

the seats. The total number of seats in the state assembly were based on a number that was twice as many as the number of members elected to the HoR from the concerned state through the FPTP electoral system. 60% members in the State Assembly were elected in accordance with the FPTP electoral system and 40% of the remaining members were elected in accordance with the PR electoral system.

State elections: The state elections in Nepal were held alongside the

parliamentary elections in two phases on November 26 and December 7, 2017 with the left alliance achieving a majority in six of the states whereas in State 2, the Federal Socialist Forum Nepal (FSFN) obtained a majority of the seats. The total number of seats in the state assembly were based on a number that was twice as many as the number of members elected to the HoR from the concerned state through the FPTP electoral system. 60% members in the State Assembly were elected in accordance with the FPTP electoral

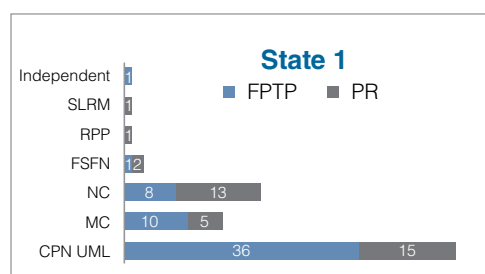
system and 40% of the remaining members were elected in accordance with the PR electoral system.

Temporary state capitals along with the Chief of States were declared on January 17, 2018 by the Sher Bahadur Deuba-led government. The seven Chief of States, five from the Nepali Congress (NC), one from the Rastriya Janata Party Nepal (RJPN) and one from the Madhesi Jan Adhikar Forum² took oath under President Bidhya Devi Bhandari on January 19, 2018.

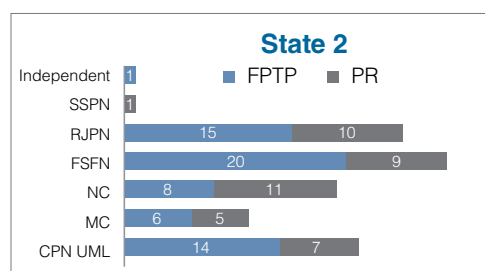
Table 3: Number of Constituencies and State Assembly seats

State	Total Number of Districts	Number of Constituencies	State Assembly Seats
State 1	14	28	56
State 2	8	32	64
State 3	13	33	66
State 4	11	18	36
State 5	12	26	52
State 6	10	12	24
State 7	9	16	32
Total:	77	165	330

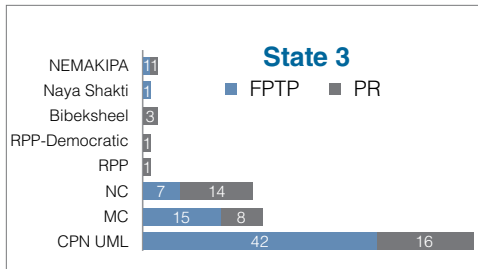
Source: Election Commission Nepal



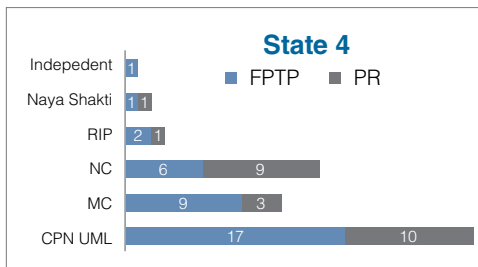
State 1	
Interim State Capital	Biratnagar
Chief of State	Govinda Bahadur Tumbahang
Chief Minister	Sher Dhan Rai
Speaker of the Assembly	Pradeep Kumar Bhandari
First State Assembly held	February 5, 2018



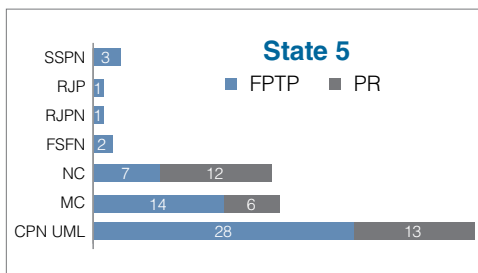
State 2	
Interim State Capital	Janakpur
Chief of State	Ratneshwor Lal Kayasta
Chief Minister	Mohammad Lal Babu Raut
Speaker of the Assembly	Saroj Kumar Yadav
First State Assembly held	February 4, 2018

**State 3**

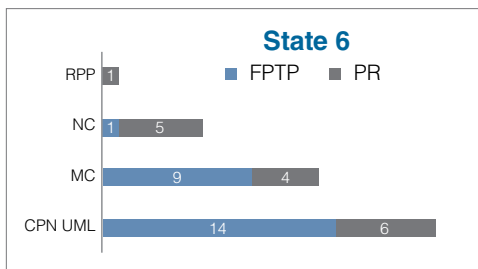
Interim State Capital	Hetauda
Chief of State	Anuradha Koirala
Chief Minister	Dormani Poudel
Speaker of the Assembly	Sanu Kumar Shrestha
First State Assembly held	February 1, 2018

**State 4**

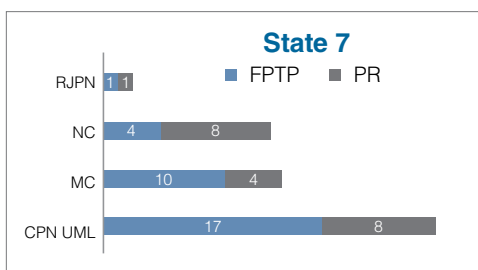
Interim State Capital	Pokhara
Chief of State	Baburam Kunwar
Chief Minister	Prithvi Subba Gurung
Speaker of the Assembly	Netra Nath Adhikari
First State Assembly held	February 5, 2018

**State 5**

Interim State Capital	Rupandehi
Chief of State	Umakanta Jha
Chief Minister	Shankar Pokhrel
Speaker of the Assembly	Purna Bahadur Gharti
First State Assembly held	February 4, 2018

**State 6**

Interim State Capital	Surkhet
Chief of State	Durga Keshar Khanal
Chief Minister	Mahendra Bahadur Shahi
Speaker of the Assembly	Raj Bahadur Shahi
First State Assembly held	February 4, 2018

**State 7**

Interim State Capital	Dhangadi
Chief of State	Mohan Raj Malla
Chief Minister	Trilochan Bhatta
Speaker of the Assembly	Arjun Bahadur Thapa
First State Assembly held	February 4, 2018

Source: Election Commission Nepal

CPN–MC: Communist Party of Nepal – Maoist Center

CPN–UML: Communist Party of Nepal – United Marxist Leninist

RJP: Rastriya Janamorcha Party

RPP: Rastriya Prajatantra Party

NC: Nepali Congress

FSFN: Federalist Socialist Forum Nepal

RJPN: Rastriya Janata Party Nepal

RSFN: Rastriya Samajwadi Forum Nepal

Minister of External Affairs of India visits Nepal:

Minister of External Affairs of India, Sushma Swaraj visited Nepal from February 1 to February 2, 2018. She conveyed the willingness of the Government of India to work closely with the Government of Nepal with the aim of further strengthening bilateral ties.³ The prime minister of Nepal Sher Bahadur Deuba paid a courtesy call to the President of Nepal, Bidhya Devi Bhandari. She also held meetings with Khadga Prasad Sharma Oli and Pushpa Kamal Dahal from the left alliance, and Upendra Yadav and Mahanta Thakur from the Madhesh based parties.⁴ The visit is significant because it is the first visit of an Indian delegation post federal elections in Nepal. Also, the patchy relations of the Government of India with the CPN-UML under the Oli-led government in 2015/16 makes this visit particularly significant in the light of the left alliance forming the upcoming government.

Nepal elected as a member of the Human Rights Council with highest votes in the Asia Pacific group:

Nepal has been elected as a member of the United Nations Human Rights Council for the first time since the creation of the Council in 2006, obtaining the highest number of votes in the Asia Pacific group. This move comes after Nepal successfully completed the local level elections. In the Comprehensive Peace Agreement signed in the post war era, Nepal's government and political parties had committed to upholding human rights as per the international law, restoring democracy, rule of law and forming the government.

Government lowers age ceiling for social security and increases allowances:

The government has lowered the age ceiling for social security by 5 years, thus entitling people who are over the age of 65 to be eligible for a social security

allowance of NPR 2000 (USD 19.41) per month. Also, children below five, locals and Dalits of Karnali region above 60 years are eligible for state benefits. NC made a commitment to increase social security during the elections. However, increasing social security allowance puts an additional burden on the country's economy, particularly considering that the country is already spending over NPR 40 billion on social security allowance.⁵

Truth and Reconciliation Committee (TRC) and the Commission for Investigation of Enforced Disappeared Persons (CIEDP) term extended by a year:

The term of the TRC and CIEDP has been extended for a year. Prior to extension, the term of the TRC and CIEDP was slated to expire on February 9, 2018. The two bodies were set up to resolve conflict issues of the war-era victims and provide transitional justice.⁶

OUTLOOK

With the federal legislature, state legislature and local legislature in place, Nepal has finally institutionalised federalism. With a government that has secured a majority in the federal legislature, local legislature and six of the state legislature, the people of Nepal expect political stability and economic prosperity in the days ahead. The alliance of two of the biggest parties of Nepal and their plan to form a unified party will be at the centre stage of Nepali politics, since accommodating several top leaders of both parties in a single party and a single government will be challenging. The country is also expected to see elections for the president and vice president in the upcoming months.

INTERNATIONAL ECONOMY

Leaders of the world's biggest economies gathered in Davos, Switzerland for the World Economic Forum Annual Meeting to discuss an array of political, economic and social issues. The uphill task of forming a coalition government is finally over in Germany. The Bharatiya Janta Party (BJP) government's impressive budget and transformational reforms may help India advance as the seventh largest economy in the world. Venezuela is facing a severe economic crisis as inflation hits record levels and the proliferation of black markets have made the life of Venezuelans difficult. Oil prices have continued to rise for the past seven months and this upward trend is expected to continue in 2018.

World Economic Forum Annual Meeting 2018 held: The 48th Annual Meeting of the World Economic Forum took place in Davos, Switzerland from January 23 to January 26 2018. The theme of the annual meeting was, "Creating a Shared Future in a Fractured World". The latest World Economic Outlook, a survey conducted and published by the International Monetary Fund, was revealed at the annual meeting. The World Economic Outlook projects that global growth for 2018 and 2019 will rise by 3.9%. Moreover, India remains the world's fastest-growing major economy, with a projected growth rate of 7.4%, ahead of China at 6.6%.⁷ The 2018 Inclusive Development Index, an annual assessment of 103 countries on eleven dimensions of economic progress, was also unveiled during the meeting and indicated that Norway is the world's most inclusive country.

India's Union Budget 2018: India's Finance Minister rolled out the Bharatiya Janta Party (BJP) led

government's full-fledged budget ahead of next year's national polls. The union budget prioritises agriculture economy where India's farmers and villagers, and agriculture based companies emerge as the biggest winners. Transport companies, consumer companies, jewelers, airports, and the government's National Health Protection Scheme are expected to benefit from this budget as well. However, the government's decision to impose a long-term capital tax on equity investment might have an effect on the financial sector. The Indian government has undertaken many transformational reforms such as demonetization, implementation of the bankruptcy code and the introduction of GST. Manufacturing and service sectors have also resumed their high growth rates. Exports are expected to grow at 15% in 2017/18. India is firmly on the verge of achieving a high growth of 8% and above. According to the Budget Estimate (BE), the fiscal deficit will remain at 3.3% of the GDP. The Indian economy is now a 2.5 trillion-

dollar economy – the seventh largest in the world.⁸

A grand coalition deal reached in Germany: European Union partners praised an agreement between Angela Merkel's Christian Democratic Union of Germany (CDU), Social Democratic Party of Germany (SPD) and Christian Social Union in Bavaria (CSU) to form a new government, but a vote of SPD members is pending.⁹ This will be the first SPD government led by a CDU chancellor. SPD will now have three major ministries – foreign affairs, finance and labour. Bavaria's CSU has been advocating a tougher line on immigration than CDU. CSU will take over the Interior Ministry. Merkel's CDU will have control over the Economy Ministry and smaller posts. Merkel said the deal would form the basis of, "a good and stable government".¹⁰ The grand coalition of political parties in Germany has been hailed as good news by European leaders and paves the path for Germany to play a leading role in the European Union.

Inflation in Venezuela world's highest at 2616% last year:

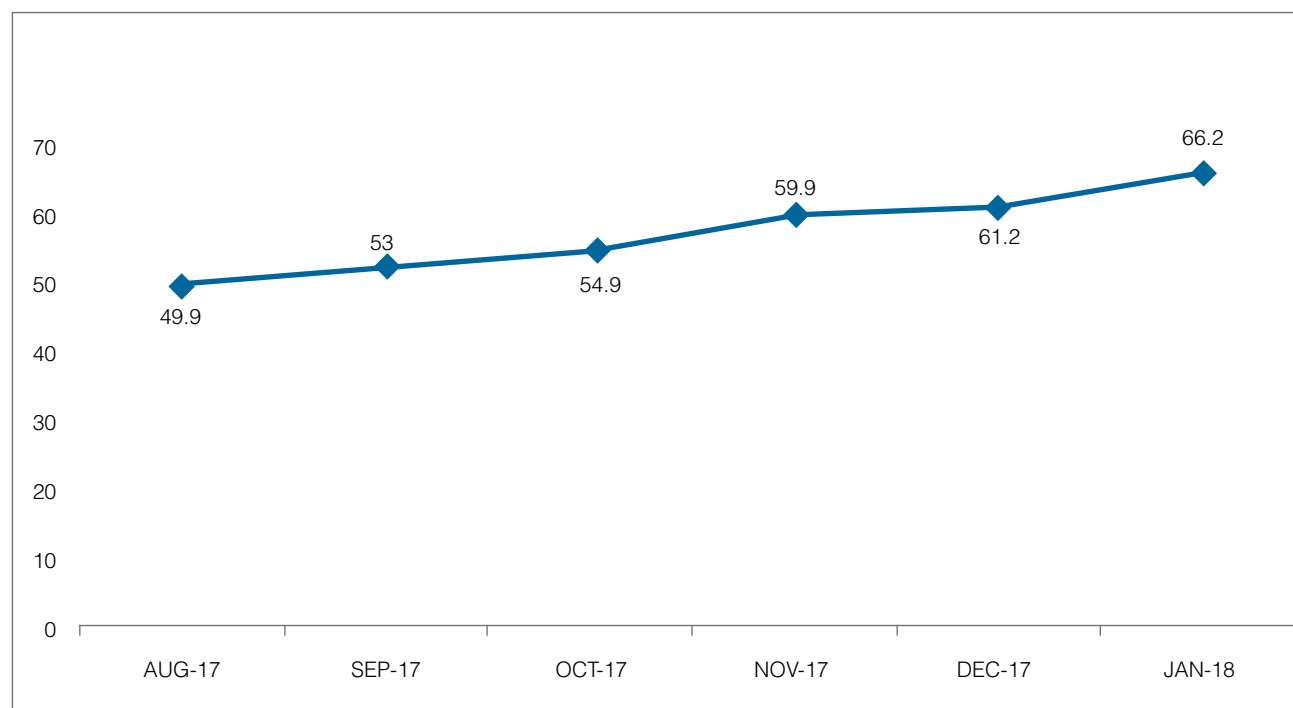
Venezuela economic crisis continues to worsen. It had the world's highest inflation levels at 2616% last year.¹¹ The country's minimum wage went up 40% in January but still is worth just over USD 2 per month on the black-market exchange. Venezuela's bolivar currency weakened about 35% against the dollar in the last month alone. Tens of thousands of people are struggling to buy food and medicine. Anger and frustration are rising and there have been a number of incidents where shops and homes have been looted. Law and order have been under serious threat. The central bank

has not published inflation or gross domestic product data for two years. President Nicolas Maduro blames the crisis on the "economic war" waged by Washington and the opposition against his government. Conversely, critics blame the government's strict currency and price controls.

Surge in crude oil prices: Crude oil prices have been on an upward trend for the past seven months, fuelled by an almost 30% increase in US natural gas prices. As per the latest commodity price data (the pink sheet) published by the World Bank, there was a sharp rise in average crude oil prices from NPR 6306 (USD 61.2) in December

2017 to NPR 6,821 (USD 66.2) in January 2018.¹² The average crude price stood at NPR 6,172 (USD 59.9) in November 2017 as shown in Figure 2. There are considerable uncertainties in the 2018 forecast for non-Organisation of the Petroleum Exporting Countries (OPEC) supply, particularly regarding an increase in US tight oil (abbreviated Light Crude Oil) production. In OPEC's Monthly Oil Market Report (MOMR) for December, growth now stands at 3.7%, up from an initial forecast of 3.2% at the start of the year. The healthy momentum is expected to continue in 2018, with growth forecasted at 3.7%.¹³

Figure 2: Monthly average price of crude oil



Source: World Bank Commodities Prices (The Pink Sheet)

OUTLOOK

During the 48th World Economic Forum Annual Meeting, the President of the United States, Donald Trump, reiterated that he will always put America first when it comes to trade negotiation deals and encouraged leaders of other countries to put their countries first. India expects to achieve high Gross Domestic Product (GDP) growth of 8% plus with the implementation of the union budget in 2018. For the first time, an SPD government led by a CDU chancellor will represent Germany, helping it to play a leading role in the European Union. Meanwhile, Venezuela is still having a hard time tackling hyperinflation. Oil prices might not fall unless shale producers increase production.



MACROECONOMIC
OVERVIEW

MACROECONOMIC OVERVIEW

The year-on-year (YoY) inflation level inflated to 4.0% over the past six months of Fiscal Year (FY) 2017/18, nevertheless the inflation is within the targeted level of 7%. On the other hand, Nepal's trade deficit continues to widen as merchandise import increased to NPR 534.16 billion (USD 5.20 billion).

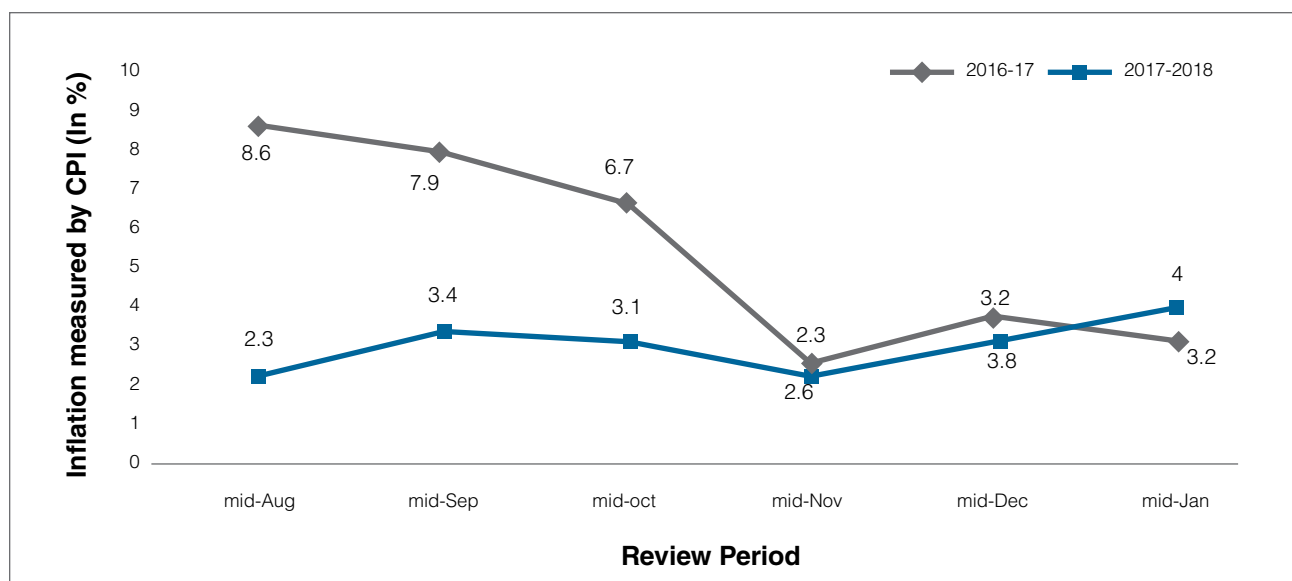
Inflation: The inflation rate, measured by Consumer Price Index (CPI), has increased to 4.0% in mid-January (see Figure 3). It stood at 3.2% over the same period in the previous year. Food inflation surged to 2.4%, which was caused by the increase in prices of pulses and legumes, spices, vegetables and fruits. Non-food inflation, however, moderated to 5.3% on the back of declining prices of clothes and footwear, furnishing and household equipment and housing and utilities.

The drop in inflation rates can be mainly attributed to an improved supply situation and a deceleration in the Indian inflation rate.

Inflation wedge between Nepal and India: The inflation wedge, measured as the YoY change in CPI of India and Nepal has fallen to -1.07%, as shown in Figure 4: Year-on-year percentage change in CPI in Nepal and India and the inflation wedge in the corresponding period for FY 2017-18. Over the same

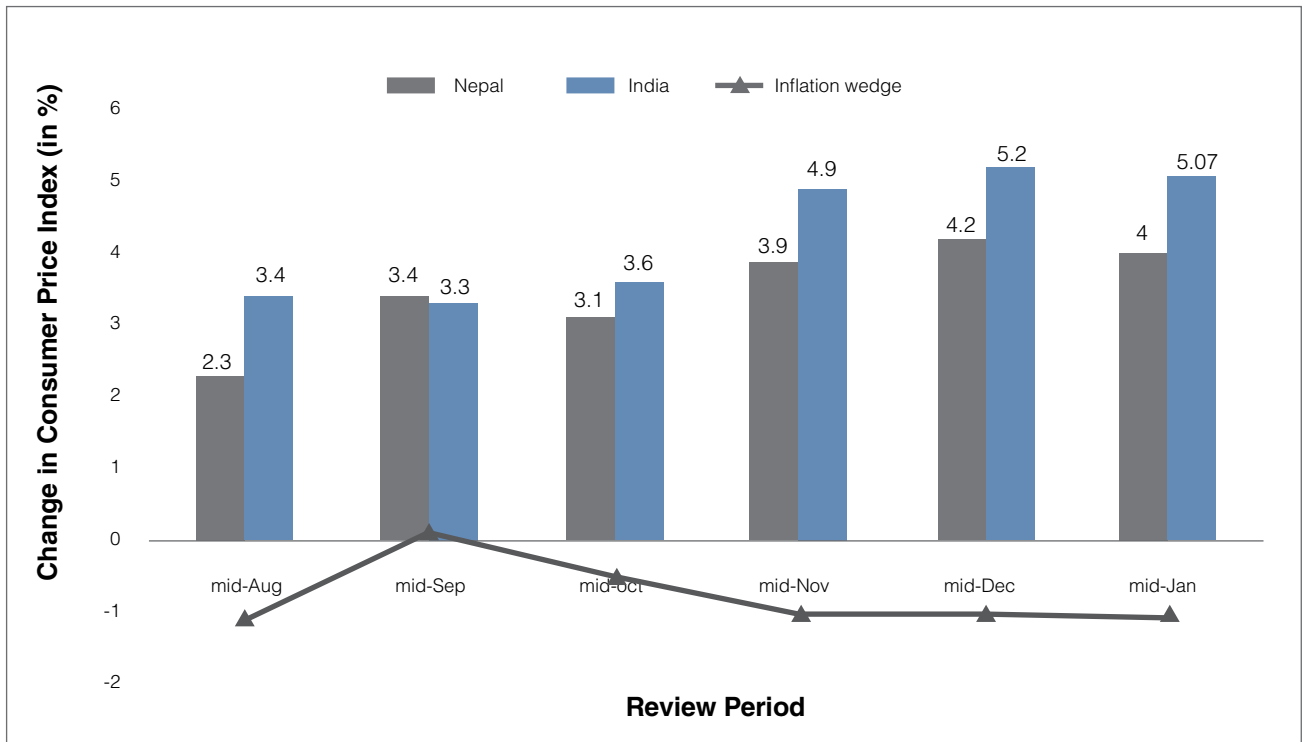
period last year, the inflation wedge between India and Nepal stood at 0% as shown in Figure 5. The inflation wedge between the two countries further decreased from -1.0% in December to -1.17% in January. An improved supply situation between the two countries and a deceleration in the Indian inflation rate can be cited as the main reasons for the subtle inflation wedge. The average inflation wedge for FY 2016/17 had stood at -0.5%.

Figure 3: Year on year inflation measured by Consumer Price Index (CPI) for six months of FY 2016-17 & 2017-18



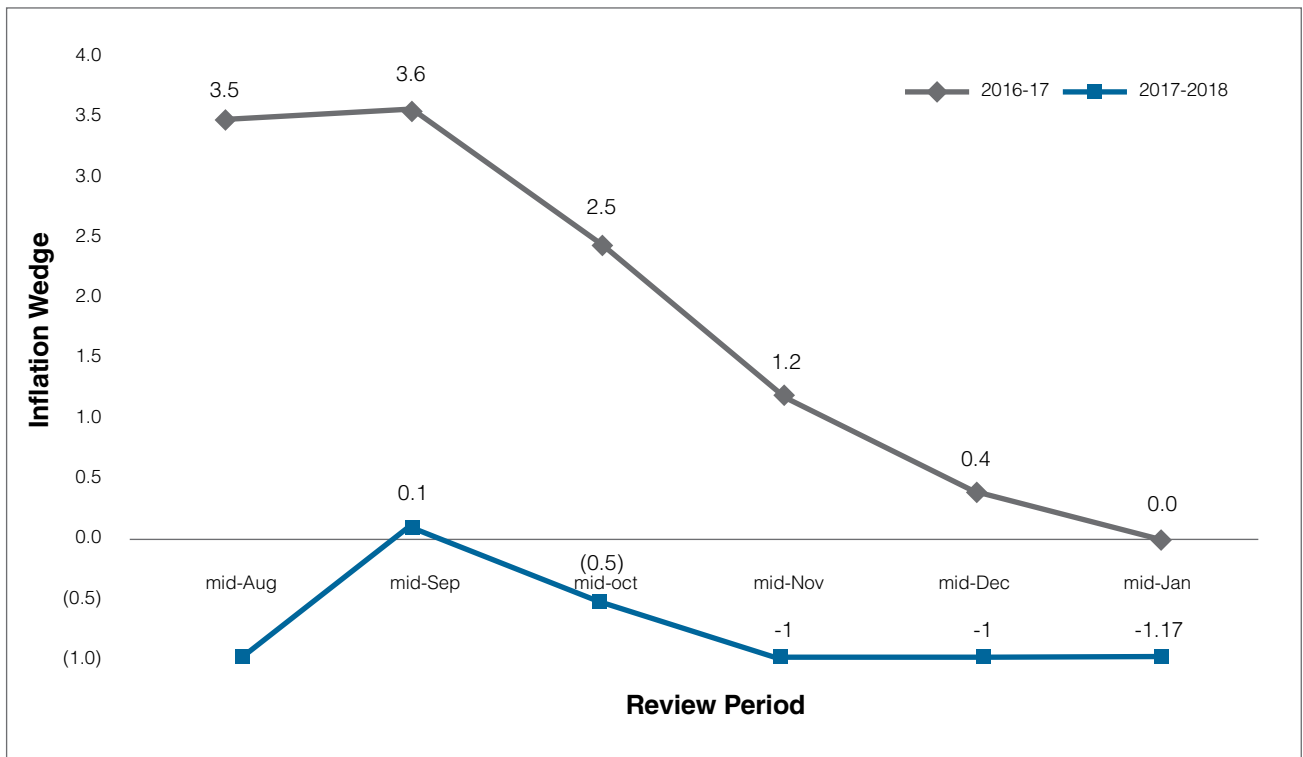
Source: Current Macroeconomic Situation of Nepal (Based on the six-month data of 2017/18), Nepal Rastra Bank

Figure 4: Year-on-year percentage change in CPI in Nepal and India and the inflation wedge in the corresponding period for FY 2017-18



Source: Current Macroeconomic Situation of Nepal (Based on the six-month data of 2017/18), Nepal Rastra Bank

Figure 5: Year-on-year change in inflation wedge (based on CPI) between Nepal and India in FY 2016-17 & 2017-18



Source: Current Macroeconomic Situation of Nepal (Based on the six-month data of 2017/18), Nepal Rastra Bank

Import-export and trade deficit:

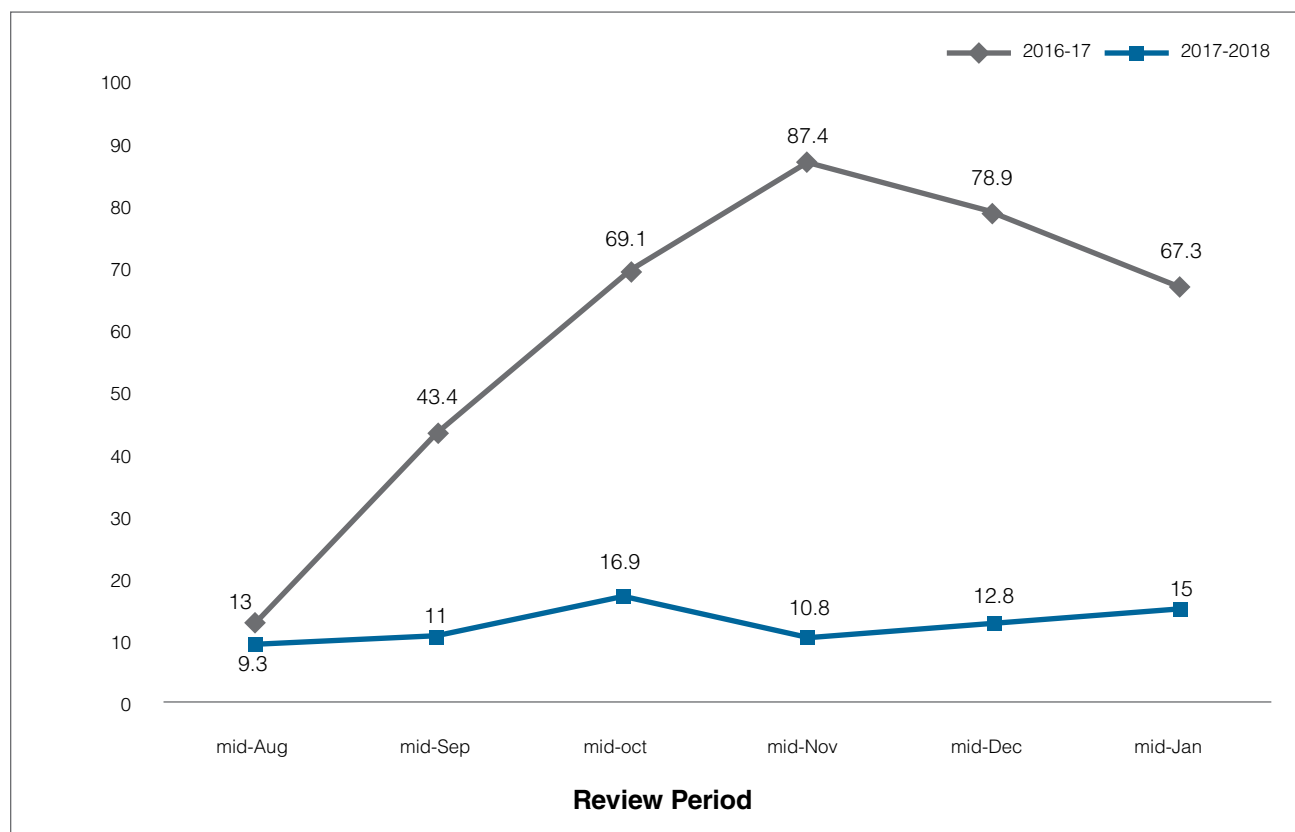
Merchandise imports have increased by 15% to NPR 534.16 billion (USD 5.20 billion) in the first six months of FY 2017/18, as shown in Figure 6 compared to 67.3% in the same period of the previous year. In comparison to the same period last year, Nepal's import from India increased by 15.3%, showing a greater dependency on its neighbour.

Merchandise exports have grown at a sluggish pace in comparison to a drastic

increment in merchandise imports. Merchandise exports increased by only 13.4% to NPR 41.14 billion (USD 399 million) in the first six months of FY 2017/18. The corresponding figure was 14.8% in the same period of previous year. A lack of growth in the industrial sector can be attributed to the lack of any substantial growth in exports. Similarly, six months average wholesale price indices (WPI) moderated to 2.0% in FY 2017/18. The corresponding figure was 1.8% in the previous year.

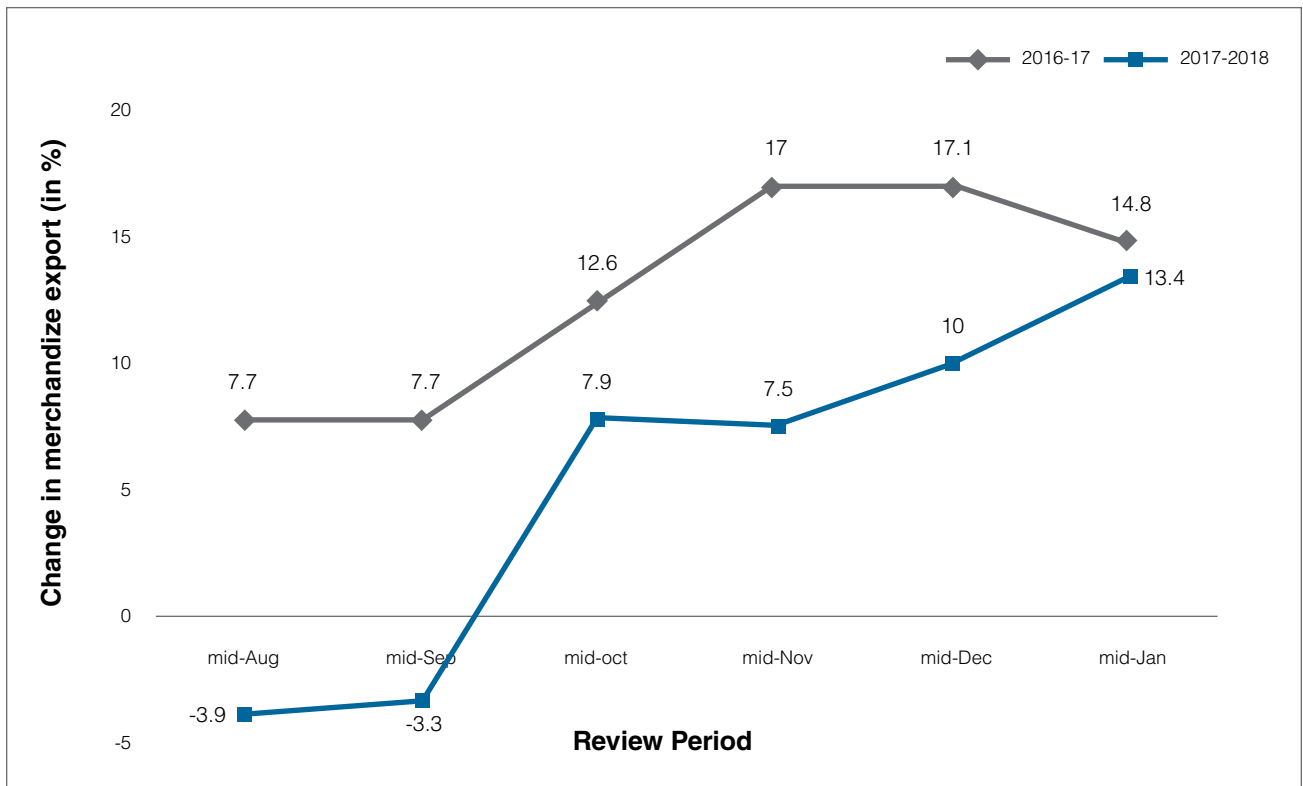
As a result of the widening gap between imports and exports, Nepal's trade deficit increased by 15.1%, compared to 74% in the same period the previous year, as shown in Figure 8. Nepal's trade deficit now stands at NPR 493.02 billion (USD 4.78 billion). Nepal's propensity to import goods from India and the lack of growth in domestic producers can be attributed to the widening trade gap. With the government unable to boost exports and support the development of the domestic industrial sector, the trade

Figure 6: Year-on-year percentage change in merchandise imports in review periods in FYs 2016-17 and 2017-18



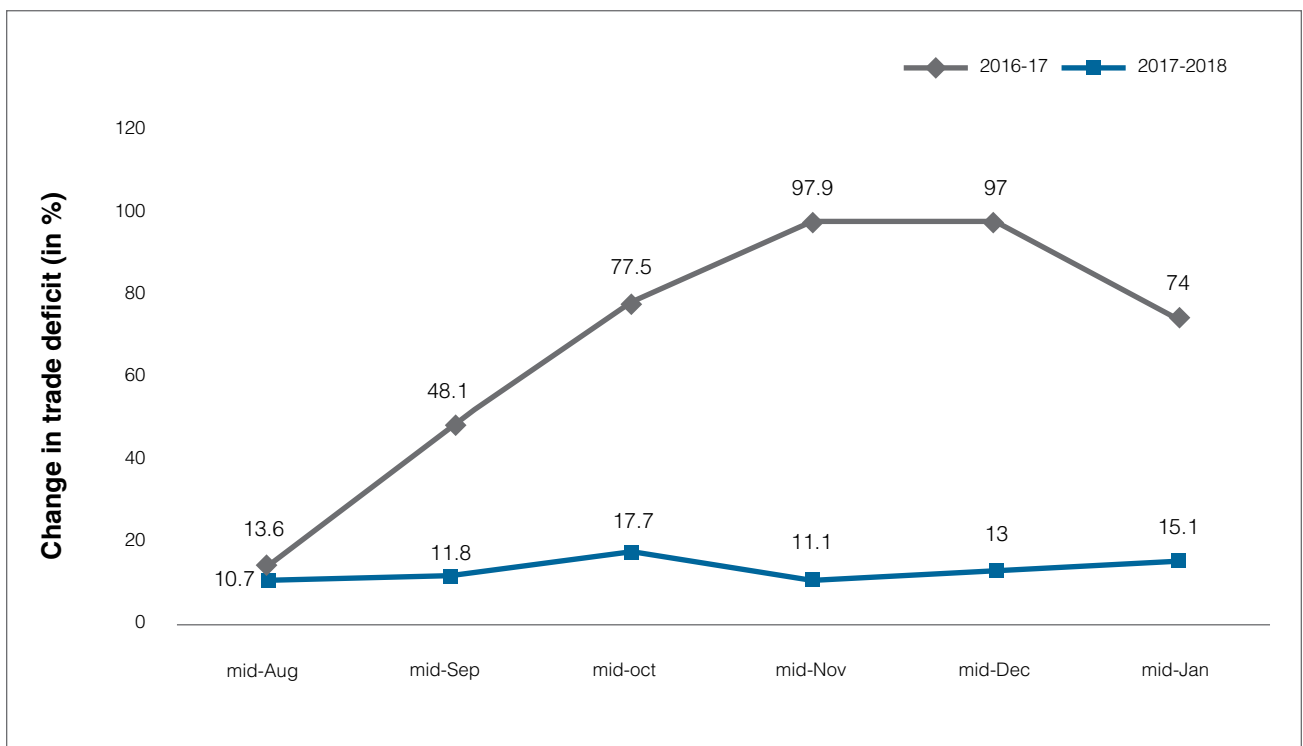
Source: Current Macroeconomic Situation of Nepal (Based on the six-month data of 2017/18), Nepal Rastra Bank

Figure 7: Year-on-year percentage change in merchandise exports in review periods in FYs 2016-17 and 2017-18



Source: Current Macroeconomic Situation of Nepal (Based on the six-month data of 2017/18), Nepal Rastra Bank

Figure 8: Year-on-year percentage change in trade deficit in review periods in FYs 2016-17 and 2017-18



Source: Current Macroeconomic Situation of Nepal (Based on the six-month data of 2017/18), Nepal Rastra Bank

deficit will continue to worsen with imports growing at a substantial rate.

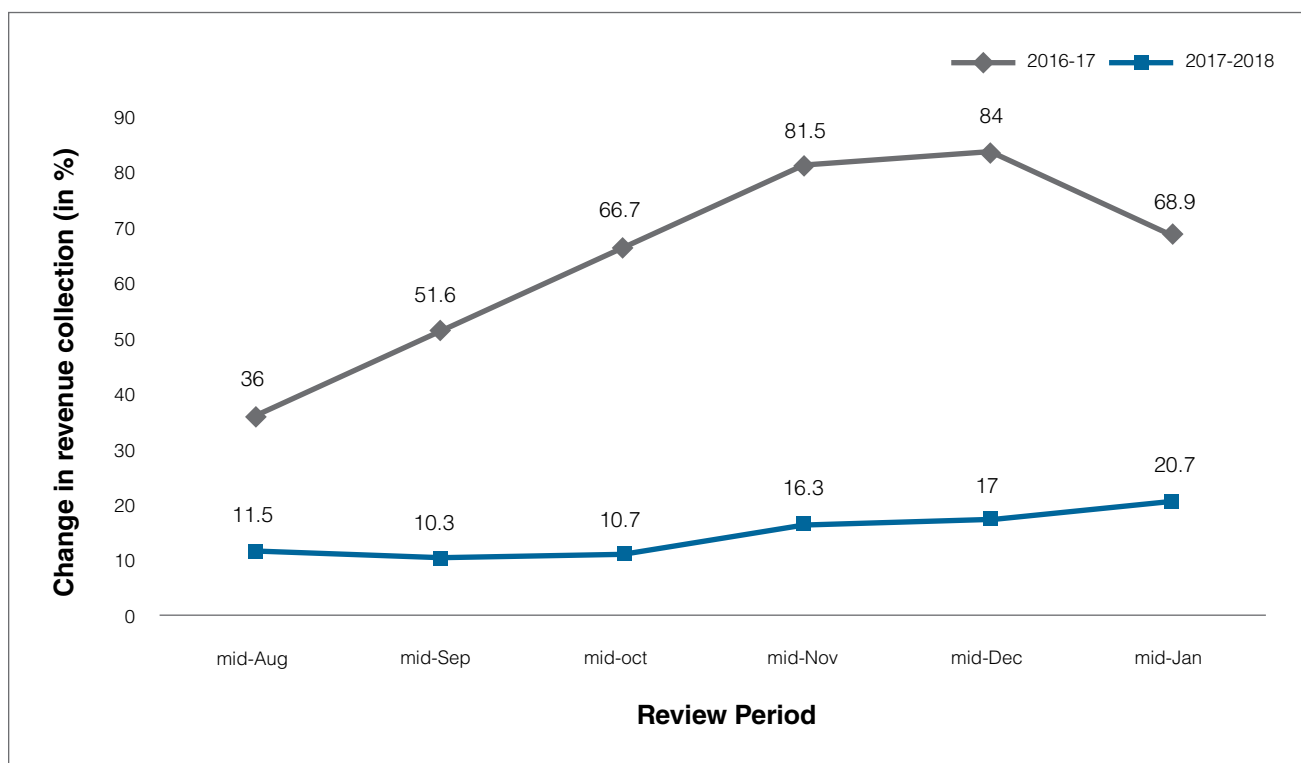
Government revenue: Government revenue collection increased by 20.7%, amounting to NPR 335.10 billion (USD 3.25 billion). The revenue collection had increased by 68.9% to NPR 277.57 billion (USD 2.69 billion) in the corresponding period of the previous year as shown in Figure 9.

Government expenditure: Total government expenditure increased by 42.4% to NPR 364.95 billion (USD 3.54 billion), compared to an increase of 27.54% in the corresponding period of the previous year, as shown in Figure 10. This was on account of both recurrent and capital expenditure rising to NPR 303.33 billion (USD 2.94 billion) and NPR 42.72 billion (USD 415 million) respectively. Recurrent and capital expenditure

stood at NPR 196.47 billion (USD 1.91 million) and NPR 30.97 billion (USD 300 million) respectively in the corresponding period of the previous year.

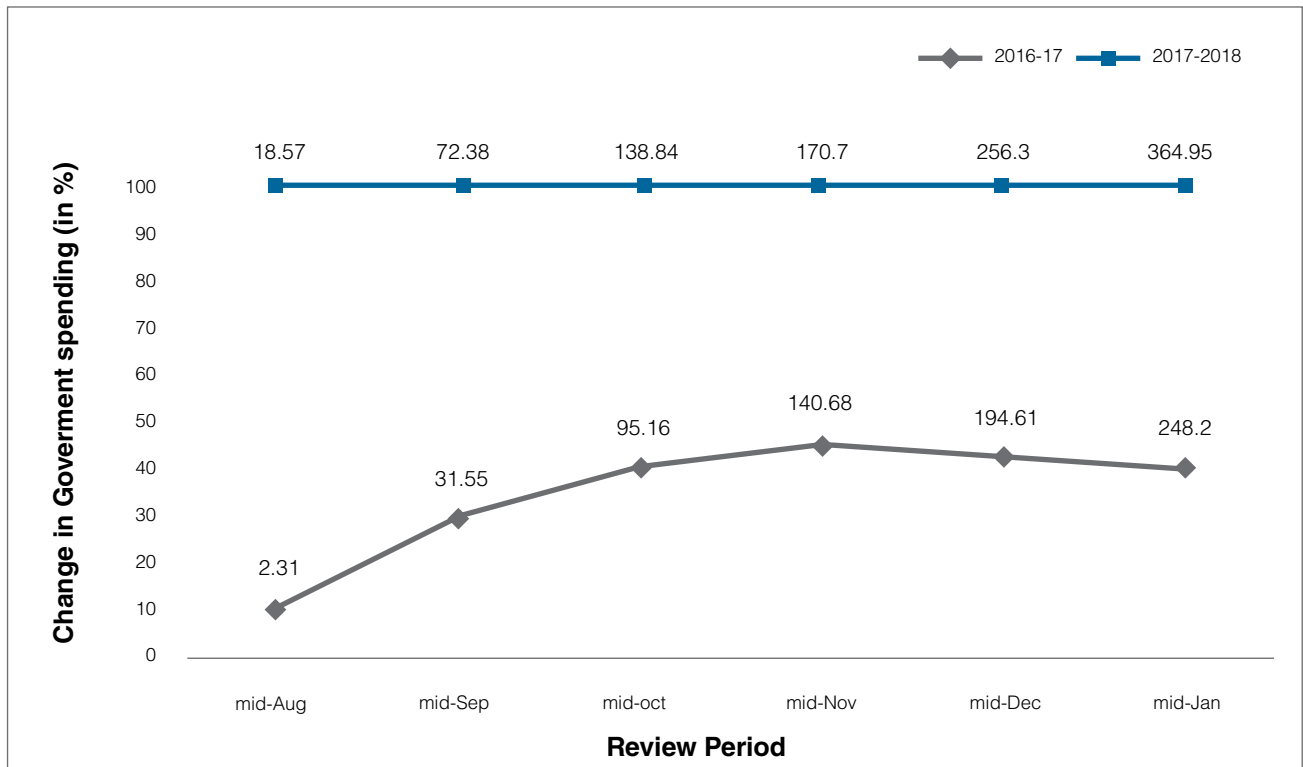
The utilisation of capital and recurrent budget has been approximately 12.75% and 37.75% respectively. Figure 11 shows the monthly outlay in terms of percentage of the target achieved for government spending.¹⁴

Figure 9: Year-on-year percentage change in revenue collection during the review periods for FY 2016-17 and 2017-18



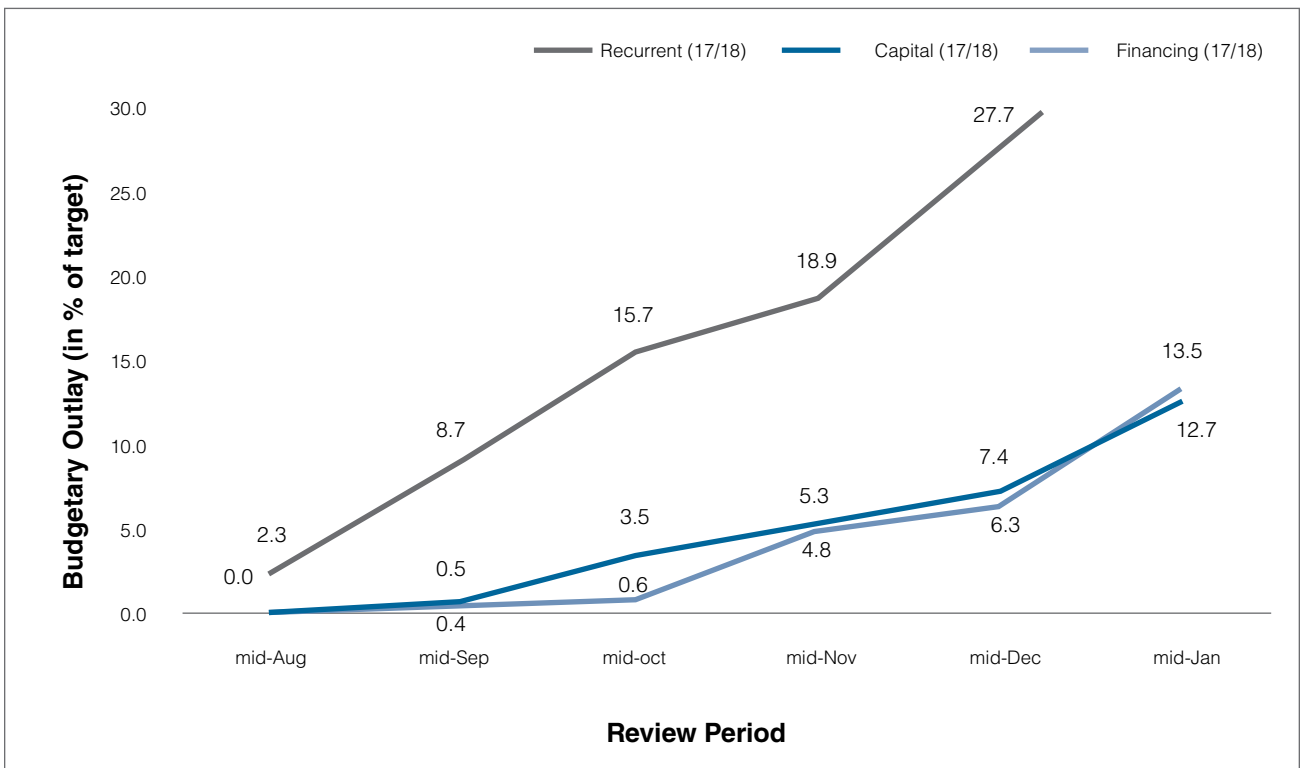
Source: Current Macroeconomic Situation of Nepal (Based on the six-month data of 2017/18), Nepal Rastra Bank

Figure 10: Year-on-year change in government expenditure during the review period for FY 2016-17 and 2017-18



Source: Current Macroeconomic Situation of Nepal (Based on the six-month data of 2017/18), Nepal Rastra Bank

Figure 11: Budgetary outlay trend over the twelve months of FY 2017-18



Source: Current Macroeconomic Situation of Nepal (Based on the six-month data of 2017/18), Nepal Rastra Bank

OUTLOOK

After a prolonged political struggle, a new government has been formed under the leadership of CPN-UML Chair KP Sharma Oli. The seemingly stable government should now prioritize the economic agenda by ensuring social harmony, rule of law and good governance. For a developing country like Nepal, increasing economic volatility has become a fact of life and therefore economic advancement should be based on sound macroeconomic policies. In this context, prudent fiscal policy will help fulfill the socio-economic aspirations of sustainable growth, full employment, optimal inflation and viable external FDI.

To achieve the aspired vision of 2030, the economy should promote export-oriented industries. Empirical findings from various countries including Mexico, Singapore, South Korea and Taiwan reveal a robust relationship between the expansion of exports and development of manufacturing industries. Additionally, the development of export-oriented industries helps increase capital efficiency, national income and overall factor productivity. Export-led growth strategy is particularly useful to smaller economies as they can expand their limited domestic market by exporting outputs to international markets. Nevertheless, both demand and supply-side effects of export promotion led growth should be considered as the adoption of such strategy by least developed countries (LDCs) can create excessive competition.

Nepal also needs to focus on new interactive notions of economic development (apart from hydro and tourism) supported by robust investments in infrastructure. Such investments in infrastructure will help mobilize economic actors ranging from financial institutions to labourers. Doing so will help Nepal achieve and sustain the year-on-year targeted economic growth of 7%-10% and considerably expand its economic size from the current USD 26 billion.

As political fragility becomes a thing of the past, Nepal can learn and emulate the economic development models of other countries such as South Korea, Malaysia and Singapore among others. The extraordinary economic upsurge of the four "Asian Tigers" (Hong Kong, Singapore, South Korea and Taiwan) was based primarily on the strong development of the manufacturing industry and equal distribution of wealth. In this regard, Nepal can prioritize the growth of indigenous small and medium enterprises (SMEs), which will concurrently help in increasing employment and exports.

Likewise, considering the demographic situation of Nepal, investments towards physical and human capital should also be prioritized. Currently, approximately 40% of the population are in the age group of 18-40 indicating that Nepal has a robust foundation of economically active human resource. However, in the next twenty years, the size of economically active population will decrease substantially. As such, the right vision and investments are required to prolong Nepal's economic development for a substantial period.

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SECTORAL
REVIEW

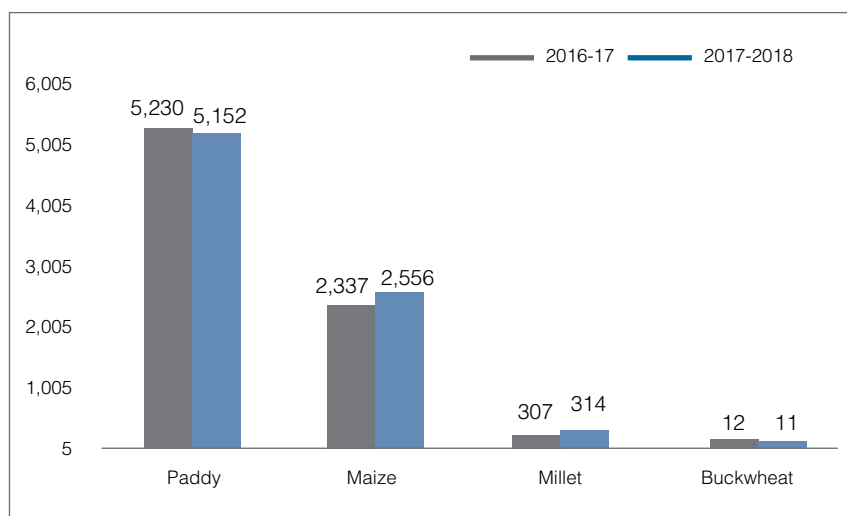
AGRICULTURE

Due to the receding agriculture output, the World Bank Group has decreased the forecast growth of agriculture output by 0.9% to 4.6%. Despite various positive developments being undertaken by the government to accelerate the growth of the agricultural sector, no significant improvement has been achieved in curtailing agriculture imports. Therefore, regulators need to endorse appropriate policies for making the country self-sufficient in the agriculture sector.

Paddy production down by 1.5% to 5.15 million tons:

The paddy production has dropped slightly by 1.50% in Fiscal Year (FY) 2017/18, while the production of maize was at an all-time high, with a near 10% increase in production. As per the Summer Crop Production Report of FY 2017/18 prepared by the Ministry of Agriculture Development (MoAD), the total paddy production of the country in FY 2017/18 was 5.15 million tons. The farming was done in 1.46 million hectares of land. In contrast, 5.23 million tons of paddy was produced by utilising 1.55 million hectares of land in FY 2016/17. The MoAD, this year, had earlier expected significant growth in paddy production, however the late monsoon and Terai floods affected the output. Accordingly, the maize production in FY 2017/18 was 2.55 million tons, the corresponding figure was 2.33 million tons in FY 2016/17. Such an increment in production is mainly attributed to the increase in plantation area. As such, the area was increased to 954,158 hectares in FY 2017/18 as compared to 924,321 hectares in the previous year. Similarly, the report also highlights that the production of millet has increased to 307,704 tons.¹⁵

Figure 12: Summer Crop Production in last two years (Production in tons '000)



Source: My Republica

Rice mills shutting down due to cheap imports:

The rice mills in Parsa and Bara are on the verge of shutting down as they are not being able to compete with cheaper Indian products. Currently, to compensate for the operating loss, many rice mills in these districts are repackaging Indian rice imported from India and selling it under their own brand. In the last four years, out of 300 rice mills, 250 have already closed their factories; while half of the remaining 50 are also finding it hard to sustain their business. Since the price of Nepali processed rice is higher

compared to Indian processed rice, consumers prefer cheaper rice that is imported from India.

Rice is imported from India through legal and illegal channels. It is difficult to import paddy from India due to the export quota set by the Indian government. Rice entrepreneurs are of the view that the customs office should either increase the fee on the import of rice from the current 8% to 10% or reduce the fees for paddy, which is at 5%. This would help the entrepreneurs compete with the milled rice that is imported from India. As

per the statistics from the Customs Office in Birgunj, rice worth NPR 998.1 million (USD 9.69 million) has been imported in the first six months of FY 2017/18, while rice worth NPR 888.3 million (USD 8.62 million) was imported during the corresponding period of the previous year.¹⁶

Agro import increase: According to the Department of Customs, imports of agricultural products during the last six-months of FY 2017/18 increased by 17% to NPR 105.22 billion (USD 1.02 billion). Nepal bought foreign farm products worth NPR 196 billion (USD 1.90 billion) in the last FY, up by 11.36% from the previous FY 2015/16. According to the statistics, cereal topped the list of agro imports, followed by edible oil, vegetables, animal fodder, and nuts and fruits. Among cereal imports, paddy and rice imports amounted to NPR 13.65 billion (USD 0.13 billion). Agro expert and scientist Bhola Man Singh Basnet cited that the import of cereal is growing largely due to the increasing demand for quality rice by the expanding middle-income population. According to Basnet, Basmati rice is imported to feed the people in Kathmandu in particular.¹⁷

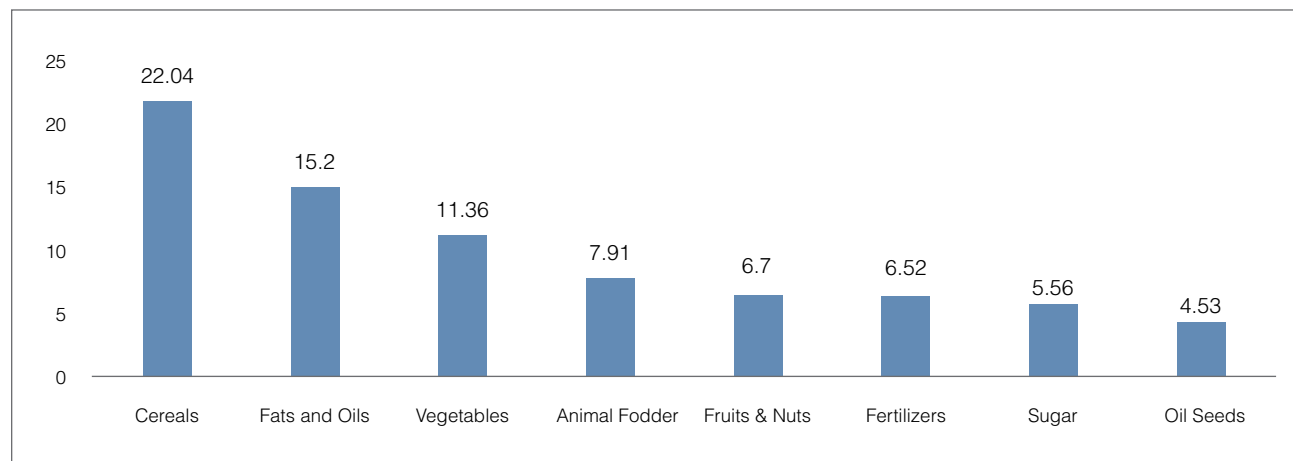
Nepali tea gets international trademark: Nepal's orthodox tea has finally received its own identity in the international market through a trademark. The tea was earlier being exported with the logo of Darjeeling, India. A new logo reflects images of mountains with the theme 'Nepal Tea Quality from the Himalaya' and a directive for the implementation of logo has been developed. In order to use the logo, tea manufacturers need to comply with a few requirements including: fully organic tea, employment security of workers, and business sensitivity towards environment protection. Tea farmers are very positive towards this development and are expecting accelerated growth and sustainability in this business.¹⁸

Nepali ginger being exported to Bangladesh: Nepali ginger exporters have found Bangladesh to be an alternate market for ginger sales. In the past one and a half months, traders have exported 35 truckloads of ginger to Bangladesh via the Fulbari-Banglabandha trade route and have 15 more trucks ready to be dispatched at the Customs Office. This is the first time in the last 10 years that Nepal

has exported ginger in this scale to a third country. Nepal produces about 250,000 tons of ginger annually and 80% of the production is exported to India. However, due to different non-tariff barriers imposed by India, the export of ginger to India has come to a complete standstill in recent days. According to the chairperson of the Nepal Ginger Producer and Traders Association, Bangladesh could be an alternate market to a portion of production but not a sole market for Nepali ginger, as the demand in Bangladesh is about only 500 truckloads as compared to production of 3,000 truckloads in Nepal.¹⁹ Ginger entrepreneurs are of the view that the government's inability to provide modern technology, knowledge, skill and investment has restricted Nepal from processing the fresh ginger into dry ginger, jam, candy, shampoo or medicine, and exporting these products to other countries to generate high values.²⁰

Supreme Court directs government to restrict use of pesticides: Considering the precarious impact of pesticides, the Supreme Court has directed the government to restrict the use of pesticides in the cultivation

Figure 13: Agro import in first six months of 2017/18 (Amount in billion)



Source: The Kathmandu Post

of vegetables. Accordingly, the Office of the Prime Minister, the Council of Ministers and the Ministry of Agriculture have been directed to immediately initiate suitable measures. The public interest litigation filed

on this issue stated that the rampant use of pesticides has been seriously affecting the health of consumers. The Consumer Protection Act, 1998 has ensured the right to consume food free of adulteration. Likewise,

the Pesticides Act, 1992 has banned the use of vegetables for a certain amount of time if they are found to be cultivated by using pesticides. However, the government has not been implementing the Act effectively.²¹

“ OUTLOOK

The agriculture output is expected to decrease due to the late monsoon and heavy floods in the Terai. The announcement in the Indian budget which assures a 50% profit for Indian farmers and plans to double their income by FY 2022 will further impede the growth of agriculture outputs in Nepal. The Indian government's proposition to provide heavy subsidies to Indian farmers' and impose non-tariff barriers has put Nepali farmers in a challenging position.

ENERGY

The Nepal Electricity Authority (NEA) mitigated load shedding and introduced various other activities under the ‘Ujjyalo Nepal Abhiyaan’ initiative. Many substations and transmission lines have been completed in the fiscal year (FY) 2016/17. The financial status of the NEA in the review period showed an operating surplus. The net loss was below NPR 1 billion (USD 9.7 million) and the nation-wide drive to reduce system losses showed positive results. The state-owned power utility is focusing on energy levelling by increasing domestic energy demand during off-peak hours. It is also working on capacity building for efficient operations and implementation of projects along with building infrastructure (hardware and software) to increase income and improve the moral health of the organisation.

NPR 204.37 billion (USD 1.98 billion) necessary to ensure electricity grid connectivity:

With the support of the National Planning Commission (NPC), the NEA Engineering Company, a subsidiary of the NEA came up with a study report showing that NPR 204.37 billion (USD 1.98 billion) is required to ensure grid connectivity throughout the country. From this amount, NPR 148 billion (USD 1.44 billion) is required for electricity generation and NPR 56.37 billion (USD 0.55 billion) is required for transmission and substations. The study was conducted over a period of 17 weeks. The NPC supported the NEA in carrying out the study on the allocation of resources in order to achieve the target of sustainable energy for all by 2030. The Vice Chairman of the NPC unveiled the study report with the hope that the NEA will be able to provide constant and optimum voltage to tap into the potential of industrialisation, provide opportunities to set up businesses and ultimately ensure quality of life,

among others. The NPC handed over the task to the NEA Engineering Company via a government-to-government contract. It is expected that once distributed, the electricity that is generated will have a low transmission loss. The generation system will be based on the load demand of the municipalities, both rural and urban.²²

Nepal’s first biogas plant starts compressed natural gas (CNG) production:

Envipower Energy and Fertilizers Private Limited, the country’s first ever biogas plant has started producing bottled CNG. CNG can be used as an alternative to liquefied petroleum gas (LPG). With cow dung, pressmud, poultry litter and biomass, the plant produces biogas which is purified and converted into CNG before it is bottled. It is the first plant in the country to produce CNG commercially. Through the use of German technology, the plant is able to produce two tonnes of cooking gas daily. NPR 220 million

(USD 2.14 million) was invested in the establishment of the plant. The company also grows maize commercially, as maize grains are regarded as the most suitable material for biogas production and can sustain the plant’s raw material requirements for longer periods. The plant is located at Sukrauli in Nawalparasi district.²³

Nepal Power Investment Summit 2018:

A three-day event, Nepal Power Investment Summit (NPIS) took place from January 27 to January 29, 2018 at Soaltee Crowne Plaza, Kathmandu. The summit was organized by the Energy Development Council (EDC), an umbrella organization representing both the private and public energy sector of the country. Major participants of the event were high level delegates from the South Asian Association for Regional Cooperation (SAARC) region, ministers, government officials, Ambassadors to Nepal, bankers, financiers and developers of energy projects. President, Bidhya

Devi Bhandari addressed the NPIS 2018 and urged domestic and foreign investors to invest in the hydropower sector as the demand of electricity is soaring in the South Asian region. The EDC claimed that participants of the summit will have access to investors willing to provide debt financing ranging from NPR 515.2 million (USD 5 million) to NPR 2.06 trillion (USD 20 billion) for various power projects related to hydro, solar and wind energy generation. In addition, the EDC also organized training programmes on engineering, procurement, construction and financing (EPCF) models to develop power projects, hydro equipment and renewable energy. These training programmes were conducted by renowned energy associations and Fortune 500 companies. More than 100 qualified hydropower projects, 20 solar power generation projects, 10 transmission line projects and 13 smart city plans were showcased at the summit.²⁴

Chameliya hydro project completed after a decade: One of the most delayed infrastructure projects in Nepal, the Chameliya hydro project, has finally started generating electricity after 10 years of its inception. The project started in FY 2006/07 and was scheduled to be completed by 2011, but completion was delayed by six years. The project has now tested production by transmitting electricity through the 132KV transmission line that connects Balach of Darchula with Attariya of Kailali district and is expected to supply electricity within a month. The 30 MW hydro project is owned by the NEA. Initially, the investment for the project was expected to be NPR 8.50 billion USD (82.5 million), but total investment rose to NPR 15.50 billion (USD 150.4 million). The Government of Nepal is the sole investor of the project. The

civil contractor of the project is the China Gezhouba Group Corporation which halted all the work in 2014 when the government refused to make an additional payment of NPR 1.09 billion (USD 10.58 million). The Chinese contractor resumed work in October 2016 and completed the construction within the extended deadline. The project site is located at Balach, Shailya Shikhar Municipality of Darchula district.²⁵

Solar power projects halt due to policy inconsistency: The NEA's 22 grid solar projects have come to a halt due to the government's policy inconsistency. The NEA planned to diversify the energy mix by launching the solar power projects with a total installed capacity of 61 MW. The NEA had already prepared a power purchase agreement (PPA) with 22 solar projects, with prices ranging from NPR 8.45 (USD 0.08) to NPR 9.62 (USD 0.09) per unit of electricity. The power purchase rate was fixed as per the guidelines of the National Energy Crisis Reduction and Electricity Development Decade declared by the government which allowed the NEA to buy solar electricity at up to NPR 9.61 (USD 0.09) per unit. The NEA selected more than half a dozen bidders who quoted prices falling within the specified range but the bidding process was halted as the Ministry of Energy changed the purchase rate to NPR 7.30 (USD 0.07) per unit. The NEA management is now waiting for the next administration to take office with the hope that it will apply a new rate. After signing the PPA with the NEA, the potential solar power developers will have to install solar plants with installed capacities ranging from 0.5 MW to 8.5 MW at 22 different locations across the country within a duration of 18 months.²⁶

NEA removes 'take and pay' provision: Under the 'take and pay' provision that was in place earlier, the NEA was bound to pay only for the amount of electricity it consumed. With the introduction of 'take or pay' provision and removal of 'take and pay' provision, the NEA now has to pay the power developer for the quantity of electricity mentioned in the PPA irrespective of whether it is able to sell the electricity or not. The Ministry of Energy has recently directed the NEA to sign more PPAs with Run-of-the-River (RoR) projects on a take or pay basis. The decision was made after the seven-year energy development plan revised the target of generating 17,000 MW in seven years up from the earlier target of generating 10,000 MW in 10 years. This has let the developers enter the generation phase after signing the PPA with the NEA. In addition, it also allowed the NEA to raise the PPA cap for RoR projects to 5100 MW up from 3000 MW. Different RoR projects with a combined capacity of 2000 MW have put forward their PPA proposals and are waiting for the response of the NEA.²⁷

PPA signed for Upper Trishuli-1 hydel project: The NEA has approved the draft PPA proposed by Nepal Water and Energy Development Company (NWEDC) for the development of the 216MW Upper Trishuli-1 hydropower project. NWEDC is a joint venture company of South Korean and Nepali investors. According to the agreement and as per the PPA guideline issued by the Ministry of Energy, NEA will purchase electricity at NPR 4.80 (USD 0.05) and NPR 8.40 (USD 0.08) per unit during the wet and the dry season respectively. It is agreed that NEA will be making payments in US dollars for a period of 10 years or until the project has repaid its foreign loans. In addition, the developer's internal rate

of return from the investment should not exceed 17%, as per the agreement. If it does exceed this percentage, then the power purchase rate should be revised and decreased. The 216 MW plant is expected to generate 1456.4 gigawatt hours of net electricity per year (1149.7 gigawatt hours during wet season and 306.7 gigawatt hours during dry season). The plant is located near Dhunche in Rasuwa district.²⁸

Gongor-Khimti transmission line project to complete soon: 220 KV Gongor-Khimti transmission line is a much-awaited project as it is to transmit the electricity that is generated from the 456 MW Upper Tamakoshi Hydropower Project. More than 70% of the construction work has been completed. The developer of the project is the Upper Tamakoshi Hydropower Company, a subsidiary of the NEA, which is also developing the hydropower project. The developer has already erected 101 towers out of

the 127 towers needed to complete the project. Likewise, it has already completed the foundation of the 20 remaining towers that are to be erected. The project office is hopeful that it will complete the project by the end of this FY. The design of the substation at Khimti is already prepared and the construction is to start within a month. The development of the hydropower project is also on track as around 93% of the construction has already been completed. The development is, however, facing some difficulties in transporting the equipment due to poor road conditions and it is likely that the completion deadline will be extended by a couple of months. The initial cost of the project was estimated to be NPR 35.3 billion (USD 342.6 million) but due to cost overruns, costs have risen to NPR 42 billion (USD 407.6 million).²⁹

Sino-Taiwanese joint venture (JV) to prepare detailed project report (DPR) of Upper Arun Hydropower

Project: The Sino-Taiwanese JV has been appointed by the NEA to prepare a detailed project report (DPR) of the 335 MW Upper Arun Hydropower project. The NEA has given the JV a time period of two years to prepare the design. The NEA had conducted a feasibility study in 1991 with the support of the World Bank and the United Nations Development Programme (UNDP) and fixed the installed capacity at 335 MW. The consultant is to optimize the installed capacity of the project. The project chief says that the plant will be built with an installed capacity of more than 600 MW, however, this will be finalized once the DPR is prepared. The project is likely to be developed under the company model as the NEA has already established Upper Arun Hydro Electric Limited, a wholly owned subsidiary. The project is crucial if the power demand is to be met, particularly in regards to East Nepal during the dry season.³⁰

Table 4: Financial performance (in NPR millions) of Nepal Electricity Authority

Fiscal Year	Total revenue	Total Operating expense	Operating Surplus	Interest expense	Net loss
2015/16	35,073.54	36,087.53	-1,013.98	5,079.73	8,890.19
2016/17	50,229.48	45,572.09	4,657.39	3,879.39	978.92

Source: Annual Report of NEA for FY 2016/17

“ OUTLOOK

Considering Nepal's RoR hydropower system, a mixture of electricity imports from India and power generated by a domestic solar and biomass system would be the best energy mix for the short term. The long-term strategy of the NEA should be focused on power quality, reliability and energy security. It has to come up with strategies to reduce operation costs, increase self-generation, maximize sales with reduction in system loss, and increase revenue from mobilisation of additional resources. Likewise, proactive efforts have to be made to adjust the electricity tariff to cover the cost of service. Distribution system augmentation is a must for a demand supply equilibrium. Once the hydro power projects (under construction) start commissioning, manufacturing industries and business complexes need to be in place to tap the electricity generated. Power trading is likely to be a challenge for the NEA. The Integrated Nepal Power System may experience a wet energy surplus and dry energy deficit situation. In order to overcome this, cross-border trading and energy banking need to be promoted. The cross-border transmission lines will enhance the possibility of power wheeling across the border and also promote energy banking and import/export opportunities.

INFRASTRUCTURE

Infrastructure development is a key driver for progress under the new federal structure. It contributes to human development, poverty reduction and the attainment of the Sustainable Development Goals (SDGs). Infrastructure will be a critical enabler of productivity and improved economic growth for each of the newly formed states.

Amlekhgunj-Raxual-Motihari oil pipeline project move ahead:

Steel oil pipes worth INR 16.6 million (USD 257,764) have been imported via the Birgunj-Raxual border. This national priority project was first proposed in 1995 and the recent imports have raised hopes that the construction for the project will begin soon. The Government of Nepal and the Government of India signed the agreement for the project in August 2015. As part of the agreement between the two governments, all construction materials imported for the project will be exempt of customs duties and fees. The project is estimated to cost NPR 4.4 billion (USD 42.7 million).³¹

Approval of Rasuwagadhi Dry Port:

The Ministry of Commerce has approved the design of the Rasuwagadhi Dry Port, giving rise to expectations that the construction of the dry port in Timure, Rasuwa will begin soon. As per the approved design, the dry port will be spread over 8 hectares of land. It will have the capacity to house more than 315 trucks and containers, while the warehouse will be built over 750 square meters. As per the agreement signed between the Government of Nepal and the People's Republic of China, China will construct the dry port and ensure that it meets international standards.³²

Imports from Rasuwagadhi are on the rise as it is considered to be an alternative gateway to China. During the first six months of the current FY, goods worth NPR 7.81 billion (USD 75.8 million) were imported through Rasuwagadhi. Similarly, goods exported through Rasuwagadhi amounted to approximately NPR 1.11 billion (USD 10.7 million).³³

Installation of electronic cargo tracking system for transit cargo:

The Ministry of Commerce plans to install electronic cargo tracking system (ECTS) on Nepal bound containers at the Kolkata port. This initiative will be supported by the Asian Development Bank (ADB). The Government of Nepal and India signed a memorandum of intent to pilot the ECTS in June 2017. The objective is to ease transit of cargo by road and rail from Kolkata via four major custom points in Nepal, namely Kolkata-Birgunj, Kolkata-Sirsiya, Kolkata-Biratnagar and Kolkata-Bhairahawa. As per the Ministry, a three-month pilot project will be launched in the initial phase. The ECTS is expected to control the turnaround time of the shipping line containers and reduce the high demurrage and detention charges being incurred by Nepali importers due to delay in return of containers to the shipping lines.³⁴

Splitting of Civil Aviation Authority of Nepal:

The International Civil Aviation Organisation's (ICAO) Universal Safety Oversight Audit Programme had recommended that the Civil Aviation Authority of Nepal (CAAN) be split into a regulator and service provider. Splitting up CAAN is one of the many components of the USD 4.2 million (NPR 432.8 million) Air Transport Enhancement Project funded by the ADB. The Integrated Civil Aviation Bill has been drafted and the law ministry has approved the draft.³⁵

Delay in upgradation of Gautam Buddha Airport may affect project funding:

As a result of the extremely slow progress in the upgradation of the Gautam Buddha Airport, the ADB has made it clear that will not finance the project further after its initial deadline ends in December. The project cost is estimated to amount to NPR 6.22 billion (USD 60.4 million). Of the total project cost, the ADB has provided USD 58.5 million (NPR 6 billion) (USD 42.75 million or NPR 4.4 billion in soft loans and USD 15.75 million or NPR 1.6 billion in grants).³⁶

Nagdhunga tunnel project detailed project report to be ready soon:

The Japanese consultant Nippon Koei is scheduled to submit the

Nagdhunga tunnel project detailed project report (DPR) by the end of February. The project is expected to cut travel time and traffic from Nagdhunga to Naubise. The project consists of the construction of a 2.45 km tunnel from Basnetchhap to Sisne Khola and a 2.6 km road

from Basnetchhap to Thankot. The project is estimated to cost NPR 20.2 billion. The Japanese government is expected to provide loans worth NPR 15.2 billion (USD 147.5 million), with repayment fixed at 40 years at an interest rate of 0.01 percent per year.³⁷

New detailed project report for Kathmandu-Terai Fast Track: The Nepal Army has decided to prepare a new DPR to develop the 76 km expressway instead of purchasing the DPR prepared by IL&FS. Currently, the Nepal Army has initiated the project based on the feasibility study conducted by the ADB.³⁸

“ OUTLOOK

Under the new federal structure, Nepal's need for adequate infrastructure such as secure energy, efficient transport, reliable communication system, is particularly important. The country's infrastructure deficit is a constraint to economic growth. The key challenge for the new provincial government will be to provide the population with reliable electricity, affordable housing and transport infrastructure, and to create job opportunities.

INFORMATION AND COMMUNICATION TECHNOLOGY

The Information Communication and Technology (ICT) sector of the country has seen major developments in recent years with the growth in internet penetration facilitated by increasing mobile connectivity all over the country. According to Nepal Telecommunication Authority (NTA)'s Management Information System (MIS) report published on February 2018, the internet penetration rate stood at 63.17%. Likewise, Nepal Telecom (NT) has the highest market share of 53.36% in terms of data/internet followed by Ncell with 42.81% market share. Meanwhile, cable and fibre networks provided by different internet service providers (ISPs) has also further stimulated the growth of internet in the country.

Adoption of online based application for driving licenses:

With the view of facilitating the general public by making it convenient for them to submit their driving license applications, the Department of Transport Management (DoTM) has initiated an online-based application system for driving licenses. Under the new system, the DoTM has fixed a quota for different zonal offices. Confirmation codes will be provided to the service seekers and the next process will start based on the code. The process of written and trial examinations will also be based on the confirmation code. Additionally, vehicles have been categorised into different groups and people applying for the driving license can choose the appropriate group through the website.³⁹

Nepal Telecommunication Authority to track down unregistered mobile phones:

In order to control the entry of unregistered mobile devices in the market via illegal channels, NTA is introducing a system under which mobile phones that are not

registered under the NTA will not accept Subscriber Identity Module (SIM) cards of telecom companies. With the mandatory requirement of International Mobile Equipment Identity (IMEI) numbers for handsets, NTA officials claim that the flow of illegal mobile phones have reduced significantly. Meanwhile, the NTA had announced that all the mobile phones need to be registered by April 1, 2017 after which the unregistered mobile phones will become dysfunctional.⁴⁰

Nepal Telecom officially connects to the Chinese internet:

India's decade long monopoly of Nepal's cyber connectivity network has ended as the Nepal-China optical fibre link has come into operation. The process of laying optical fibre cable between Kerung in China and Rasuwagadhi in Nepal has now been completed, and commercial operation of the optical fibre project has commenced. Nepal will now no longer have to depend on Indian Telecom Companies such as Bharti Airtel and Tata Communications Ltd for internet

connectivity. According to Nepal Telecom (NT), the Chinese fibre link via the Rasuwagadhi border will have a speed of 1.5 GB per second which will be increased in the near future.⁴¹

Prepaid system soon to be introduced for landline phone service:

With the view of switching all the telecom services to a real-time billing system, NT is planning to introduce a pre-paid system for its Public Switched Telephone Network (PSTN) service, also known as the landline phone service. With the new system, users will be required to deposit a certain amount before using the PSTN service and they will not be able to consume the service beyond the credit limit. The consumers will be able to determine their credit limit and the service will be disconnected automatically after the expiry of the credit limit.⁴²

Foreign telecom companies purchasing request for proposal from the telecom regulator:

With the view of promoting a culture of sharing telecommunications

infrastructure in Nepal and bringing down the cost of telecommunication services, the telecom sector regulator sought request for proposals (RfP) from both domestic and international

firms to provide a telecommunications infrastructure service in Nepal. Eight foreign firms from countries like the United States, India, China, Lebanon, Nigeria and Malaysia purchased the

RfP from the NTA, expressing their interest to provide such a service. In the initial phase, NTA plans to issue the infrastructure service license to two eligible companies.⁴³

“ OUTLOOK

During the review period, the ICT sector of the country witnessed major developments, including the official connection established to the Chinese internet. Such connectivity is expected to bring uninterrupted connections and reliable internet services in the coming days. Likewise, the government is gearing up to issue telecom infrastructure service licenses to both foreign and domestic firms, which is expected to substantially reduce the cost of telecom services in Nepal.

REAL ESTATE

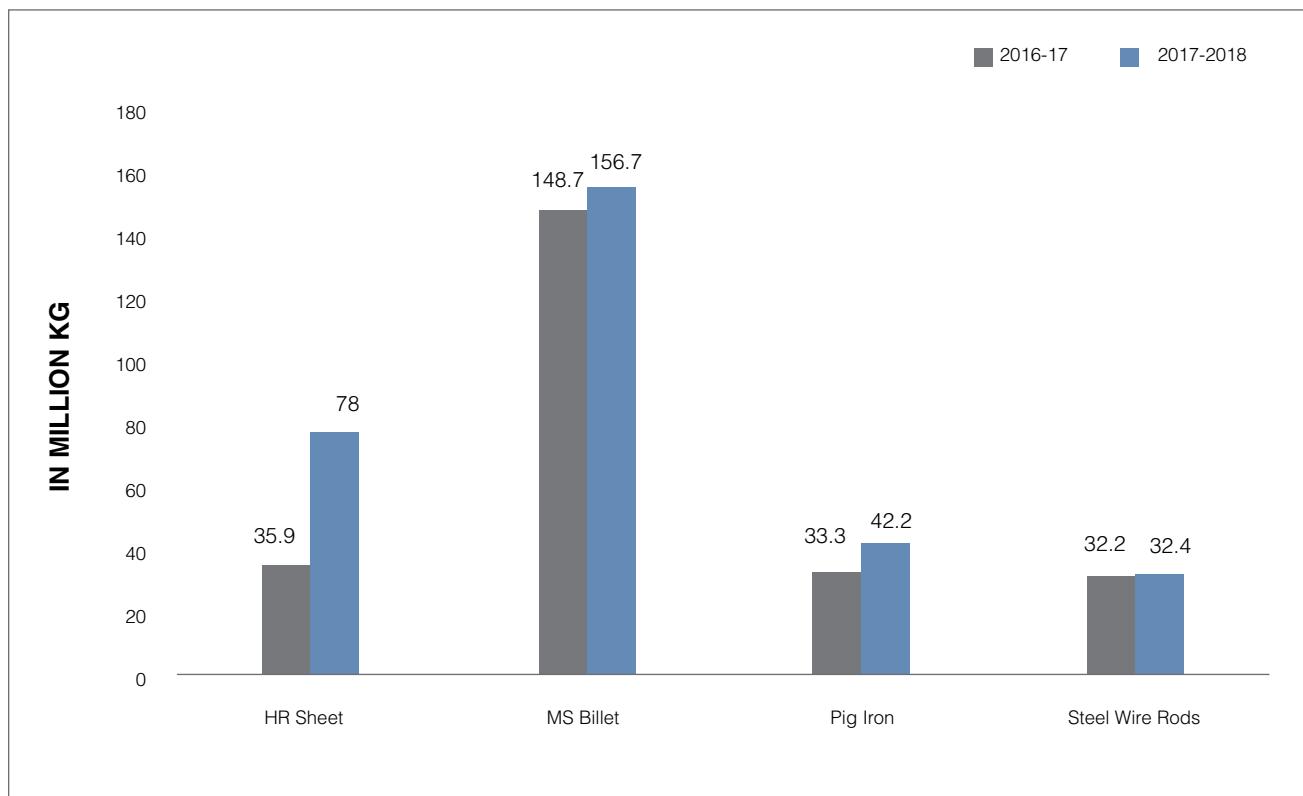
Housing and real estate represents a significant portion of most people's wealth and this is especially true for many people in Nepal. It is estimated that many Nepalis have their net worth tied up in real estate. The size and scale of the real estate market within the Kathmandu Valley make it an attractive and lucrative sector for many investors in Nepal.

Rise in import of raw material for building construction: With post-earthquake reconstruction and other construction work gathering pace, imports of raw materials

for construction have increased. Import of HR sheets (Hot Rolled) increased by 117%, amounting to NPR 4.21 billion (USD 40.8 million) during mid-July to mid-

December. During the same period, imports of MS billets increased by 5.4% to 156.7 million Kgs. Figure 14 below shows the import of raw materials.⁴⁴

Figure 14: Raw material import



Source: Department of Customs, Nepal

Increase in land and house registration: Land and house transactions has increased over the last three Fiscal Years which has increased the government revenue. Table 5 below show the trend of revenue collection

and land and building for last three fiscal years.

Kathmandu, Pokhara and Dhangadi witnessed a decrease in the approval of house designs by 3.3% 9.9% and

18.2% respectively. However, cities such as Biratnagar, Janakpur, Birgunj, Siddharthanagar and Nepalgunj witnessed an increase in the approval of house designs by 28.6%, 15%, 7.9%, 12% and 26.9% respectively.⁴⁵

Table 5: Comparative figures

Detail	FY 2014/15	FY 2015/16	FY 2016/17
Land and house registration	715,190	749,310	816,789
Design approval of permanent buildings	26,673.1	39,627.1	52,476.1
Land and house registration revenue (In NPR billion)	9.8 (USD 95.1 million)	13.8 (USD134 million)	19.3 (USD 187 million)

Source: The Himalayan Times

“ OUTLOOK

Despite the credit crunch faced by the financial sector during the last fiscal year, transactions of land and buildings increased in the country. The increase is largely driven by remittances as well as by the fact that a large section of the people is investing in land as a form of savings. However, the availability of affordable housing is a long way from making housing accessible to all. Land and housing is becoming more and more unaffordable as a result of excessively high prices of land as well as building materials.

EDUCATION

A United States Agency for International Development (USAID) report has highlighted the need for gender-targeted programmes to combat the problem of adolescent girls dropping out of secondary school. A 15-member expert panel has also made recommendations for education sector reform and has submitted their report to the government. Unhappy with the recommendations, umbrella bodies of private schools have warned against their implementation. Meanwhile, the high-level commission that was formed by the government and tasked to restructure the education system in line with the federal structure has also submitted its recommendations. As school education comes under the purview of local authorities, there are signs of a power struggle between the Ministry of Education (MoE) and local bodies, with the former accusing the latter of working without proper coordination with the ministry. The MoE, in turn, has been accused of being uninterested in working with local authorities.

Study highlights gender-specific barriers in accessing education:

A study commissioned by USAID, “Nepal Adolescent Girl’s Empowerment Assessment 2017” highlighted the critical barriers that adolescent girls face in accessing education. School dropout rates were found to peak in grades 8 and 10 for both girls and boys. Lack of money for school-related expenses and stress from parents’ economic or alcohol-related problems were found to be the most salient drivers of secondary school dropout for both genders. In addition, girls faced gender-specific barriers in completing their secondary school education, including heavy burdens or household chores, arranged marriage and elopement, menstruation and parents’ unequal treatment of daughters compared to sons and a failure to value their education. The report highlighted the need for gender-targeted programmes that focus on addressing social

norms relating to arranged marriage, menstruation and the value of girls’ education to address the problem of secondary school dropout rates.⁴⁶

Expert panel proposes education reforms, umbrella bodies unhappy:

In a report submitted to the government, a 15-member panel of education experts has proposed that local and provincial (state) governments should each contribute local content that will amount to 20% of the school curricula, while the central government should contribute the remaining 60% of the school curricula. The panel has also asserted that local and provincial governments should provide free and compulsory education.⁴⁷

In addition, the report has suggested a five-pronged approach to education sector reform including bringing schools under the complete purview of the government.⁴⁸ Unhappy with the

panel’s recommendations, the Private and Boarding Schools’ Association Nepal (PABSON) and the National Private and Boarding Schools Association Nepal (NPABSON) held a joint press conference where they accused the expert panel of trying to undermine their contribution to the education sector. They also declared that they would not allow the report’s recommendations to be implemented and instead suggested that the panel incorporate 26 of their suggestions, one of which was to ban the opening of new schools.

High-level commission submits recommendations to the Education Minister:

The 65-member high-level education commission (HLEC) formed by the government has submitted its report to the Education Minister. The HLEC was formed to help in the task of restructuring the education sector in line with the federal structure. The commission has

recommended creating an umbrella service to recruit teachers and staff for the country's universities through a rigorous, competency-based process. The report also suggests maintaining a system to frequently track the quality of candidates and appointed teachers.⁴⁹

The report strongly advises the government to take actions to bridge the gap in the quality of education between public and private schools. The report recommends that schools should not be allowed to take in foreign investments or to teach foreign curriculums. Schools for the children of diplomats should only be allowed to operate for a certain period and Nepali students should not be allowed to join these schools. The report also recommends that local authorities should make native language classes mandatory at the school level.⁵⁰

Department of Education to facilitate local governments in holding grade 8 exams: The Department of Education (DoE) has instructed its subordinate offices to support local bodies in conducting grade 8 examinations that are scheduled for March 2018. Under the federal arrangement, local level units are responsible for conducting grade 8 exams, provincial governments are responsible for the Secondary Education Examination (SEE) and the Central Examination Board (CEB) is responsible for conducting grade twelve exams. To help local bodies conduct grade 8 exams, District education officers (DEOs) who have decades of experience in conducting these exams will be transferred to the local levels.

Handover of power to local bodies creating confusion, conflict: Six months after the government

endorsed the Local Level Governance Act, which gave local bodies the authority to manage teachers, staff and education up to Grade 8, DEOs are yet to hand over power to local bodies.⁵¹ While DEOs are technically defunct under the new system, the government's failure to transfer staff to the local levels has created confusion regarding the jurisdiction of DEOs.

The move towards federalism has also caused a rift between the MoE and local bodies. So far, the MoE has released 60% of the government allocated budget of NPR 131 billion (USD 1.27 billion) to local bodies. MoE officials, however, have accused local bodies of acting without necessary coordination with the ministry. MoE officials in turn have been accused of being uninterested in working with local bodies and of preferring to work under the old centralised system instead.⁵²

“ OUTLOOK

The move towards federalism has presented both opportunities and challenges for the education sector. On the one hand, federalism provides an opportunity to bring about much needed reforms to public education. The high-level education commission formed by the government stressed the need for the government to work with both public and private institutions to maintain equity among students of different backgrounds. A separate panel of education experts recommended a five-pronged approach to education sector reform, including bringing schools under the complete purview of the government. However, it is unlikely that these recommendations will be implemented given the strong opposition from umbrella bodies of private schools who have significant political influence in the country. Moreover, lapses in the implementation of the Local Level Governance Act has caused confusion regarding the roles and responsibilities of old versus new structures. The transfer of power to the local and provincial levels has thus been, and will likely continue to be, a slow and bumpy process.

HEALTH

Although the government is making efforts to improve the health sector of the country, Nepal still lacks adequate health infrastructure to implement these efforts. Despite the government's efforts to eradicate various diseases such as leprosy, the number of victims of this disease is constantly on the rise due to a lack of awareness about personal hygiene and the disease's mode of transmission. Therefore, improvements in the health sector are only possible if the government is able to strictly implement its policies and programmes.

Arrest of 17 people on charges of illegally working as doctors: The Central Investigation Bureau (CIB) conducted raids in five hospitals in Kathmandu in coordination with the Nepal Medical Council (NMC) and the Forum for Protection of Consumer Rights Nepal (FPCRN). 17 people were arrested for illegally practicing medicine in the country. Most of those who were apprehended were Chinese nationals. They were found to be working as doctors without operating licenses from the NMC.⁵³

Increasing cases of viral fever in the Kathmandu Valley: According to the clinical research unit co-ordinator at Sukraraj Tropical and Infectious Disease Hospital, 80% of the patients visiting the hospital were found to have been suffering from viral fever. Those patients who visited the hospital complained about having sore throats, headaches, fever, coughs and colds, and breathing difficulties. The children and the elderly are the ones who are mostly affected by viral fever. Such infection is mostly transmitted through direct contact with infected individuals and

contaminated objects, and through the inhalation of virus laden air.⁵⁴

Telemedicine services to be launched: In order to ensure that health services are available to people in rural areas, Bir Hospital is set to launch telemedicine services. The hospital has already set up the infrastructure required to launch this service. Telemedicine uses telecommunication technology to deliver healthcare services to patients in remote areas. With the launch of the service, doctors in remote areas will be able to use video conferencing to consult specialists in Bir Hospital. This will save time and reduce costs for people living in rural areas as they will not have to travel over long distances for treatment.⁵⁵

Cancer registry launched across the country: In order to collect data on cancer patients all over the country, the Nepal Health Research Council (NHRC) has launched the population-based cancer registry (PBCR). Currently, the PBCR is in use in seven hospitals. However, the Ministry of Health has plans to expand the use of the PBCR to all health facilities. The

registry will help to assess the current prevalence of cancer, and will assist in projecting future cancer trends. The ten year data from the registry shows that in the year 2003, a total of 3,251 patients were diagnosed and treated for cancer. Meanwhile, in 2012, a total of 7,212 patients were diagnosed and treated. The registry also showed that in 2014, Kathmandu topped the list of ten most cancer-affected districts. Likewise, lung cancer was the most widespread form of cancer among Nepalis.⁵⁶

Rising leprosy cases in the country: Leprosy cases have been increasing in the country over the past two years. According to the Leprosy Control Division, in 2015/16, the number of leprosy patients stood at 5,641 and this number increased to 5,922 in the year 2016/17. The number stood at 5,477 in the year 2014/15. There has been a rise in the number of leprosy patients mainly due to lack of awareness, poor personal hygiene and sanitation, and low economic status. Amongst the 22 leprosy-affected districts of Nepal, the disease is mostly prevalent in the 18 districts of the Tarai region. Meanwhile, the

government has allocated a budget of NPR 3 million (USD 29,000) for 14 leprosy-affected districts.⁵⁷

Cancer, renal and paralysis patients to receive allowance: A cabinet meeting held on December 28 approved the proposal of providing a monthly government allowance of NPR 5,000 (USD 49) to the families of patients suffering from cancer, kidney failure and paralysis caused by spinal injuries. According to the chief of the Curative Service Division at the Ministry of Health (MoH), a work plan will soon be developed for this purpose. A health security fund has been proposed that will collect taxes levied on tobacco and liquor products. Allowance to the patients will be provided through this fund.⁵⁸ However, the Ministry

of Finance (MoF) has not approved this plan; the MoF has stated that the budget cannot be issued without proper guidelines and without a list of persons affected by the diseases. As a result, the MoH has prepared a draft guideline and discussions have been going on regarding the reimbursement mechanism.⁵⁹

National Health Policy 2074 drafted and submitted: A draft of the National Health Policy 2074 has been submitted to the Health Minister and it will be presented to the cabinet for approval. The objective of this policy is to improve the health and well-being of people in all the local levels of the country through the mobilisation of necessary resources. This policy ensures that basic health care services are easily accessible to people in each state.⁶⁰

Health Profession Education Ordinance issued: The Health Profession Education (HPE) Ordinance has been issued by President Bidhya Devi Bhandari. This Ordinance was promulgated in accordance with Article 114(1) of the Constitution of Nepal. However, Parliament had to endorse it within 60 days after the first House meeting. Although the government recommended the ordinance on October 23, Parliament dissolved in October 14 was not able to endorse the HPE Bill as a result of opposition from the CPN-UML and CPN (Maoist Centre). The provision of the HPE Bill regarding a moratorium of ten years on establishing new medical schools in Kathmandu Valley has been retained by the Ordinance.⁶¹

“ OUTLOOK

During the review period, the health sector of the country witnessed a series of positive developments including the issuance of the HPE Ordinance and the submission of the National Health Policy 2074. Such moves from the government are expected to bring improvements in the health sector in the coming days provided that the policies are effectively implemented. Meanwhile, as the country has moved towards a democratic federal republic form of government, the budget will be disbursed at the local level. As a result, developments in the health sector are also expected to take place from the local level in the upcoming days.

TOURISM

The Golden Jubilee celebration organized by the Nepal Association of Tour and Travel Agents (NATA) in 2016 was held with the theme “Nepali Tourism Industry of National Priority” and aimed to revitalise the government agenda of prioritizing the tourism sector. However, despite this call for prioritisation of the tourism sector, Nepal is still waiting to hit the magic figure of one million tourists. The number of tourists may be on the rise, but in order to see them rise further, the state of tourism infrastructure has to be improved. After the historic local elections last year, the mayors of different municipalities have already unveiled the plans for tourism development in their respective areas. Furthermore, this year, Nepal will host a conference on Accessible Tourism, the first of its kind in Nepal, and a Homestay Scheme Promotional Program that has grabbed the attention of the international media and tourists.

Targeted arrival of one million tourists still a dream:

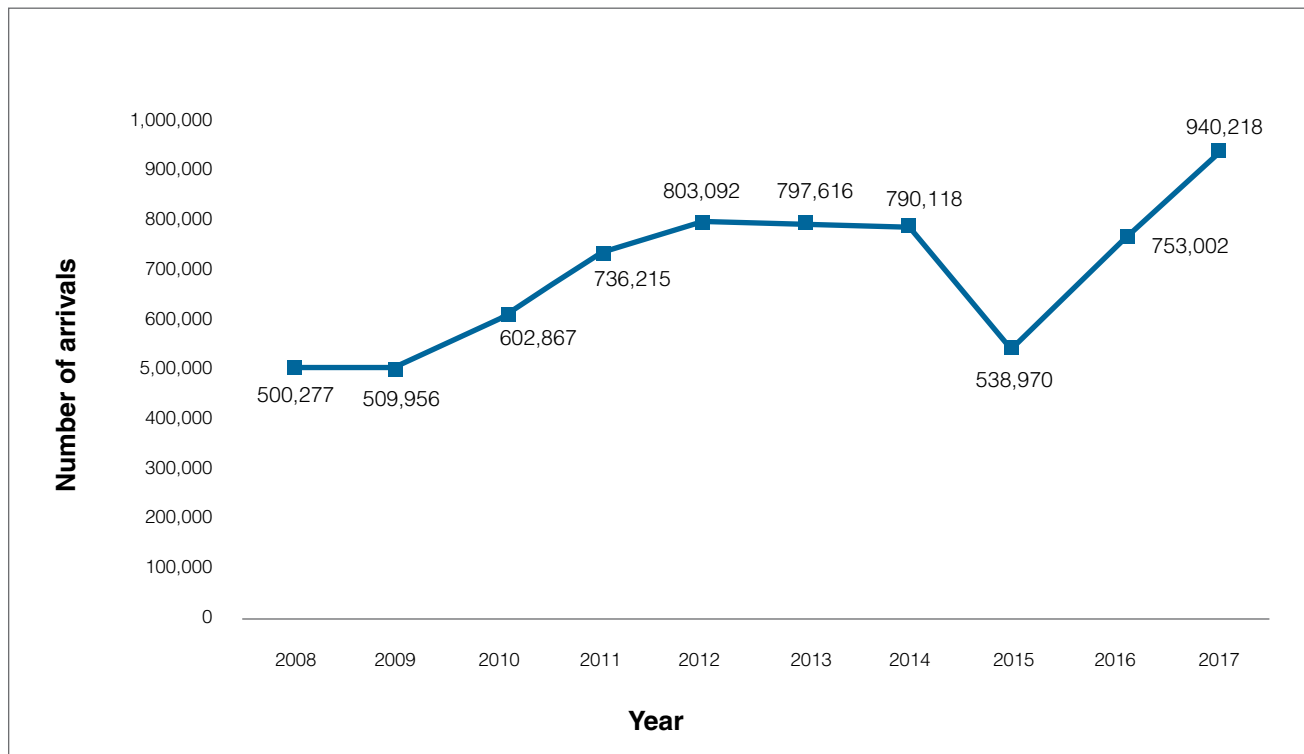
The Nepali tourism industry failed to achieve the magic figure of one million tourist arrivals in 2017. According to the Department of Immigration, the number of tourists jumped 24.86% to 940,218 individuals in 2017. India was Nepal's largest source of tourists, and the arrival of Indian tourists rose 36% to 160,832 individuals.⁶² Similarly, arrivals from China rose to 104,664 individuals in 2017, making it Nepal's second-largest source of tourists. Likewise, Nepal recorded sizeable arrivals from the United States, Australia and Japan. Arrivals from the European countries, namely the United Kingdom, Germany, France and Spain, bounced back in 2017. Due to an economic recession in most parts of Europe, tourist numbers had been declining since 2011 but now seem to be on the rise again. Moreover, the country saw the highest tourist arrivals in October,

hitting an all-time high of 112,492 individuals. November, which is considered to be the country's peak tourist season, saw the entry of 99,804 arrivals, which was lower than expected. During the peak monsoon period, and most particularly in July, the country recorded the lowest tourist arrivals. Figure 15 showcases the tourist arrivals in Nepal over the past nine years.

Three Mayors unveil plans for tourism development:

Mayors of Pokhara-Lekhnath Metropolitan City, Lalitpur Metropolitan city and Ratnanagar Municipality unveiled plans and strategies for promoting tourism in their respective areas at the Golden Jubilee Valedictory Ceremony held by the Nepal Association of Tour and Travel Agents (NATTA) in Kathmandu. Narayan Ban, Mayor of Ratnanagar Municipality stressed that his municipality has planned to declare Sauraha – a popular destination in

the country for jungle activities – a vehicle-free zone.⁶³ The Mayor and his team are also thinking of introducing small vehicles for jungle safaris as animal rights activists have criticized elephant-back safaris. The Mayor also added that the municipality will introduce a policy that bans the construction of buildings that have more than two and a half floors. Similarly, Chiribabu Maharjan, Mayor of Lalitpur Metropolitan City emphasized the commitment to complete the reconstruction of quake-damaged monuments and heritage sites within the next three years. Maharjan highlighted the need to preserve culturally-rich and historic villages like Bungamati, Khokana and Harisiddhi, among others. Maharjan also unveiled a plan to introduce an entrance fee for tourists that would be valid for a period of 72-hours. Likewise, Man Bahadur GC, Mayor of Pokhara-Lekhnath Municipality pointed out that the metropolis

Figure 15: Tourist Arrival in Nepal

Source: Department of Immigration Nepal

intends to develop Pokhara as a 'cycle city' to attract more tourists. As a strategy to promote tourism in the Pokhara-Lekhnath Municipality, catchy slogans like 'cave to cave cycling' and 'lake to lake cycling' are being used.

Nepal to host conference on accessible tourism: Nepal will host a conference on accessible tourism. This conference will be the first of its kind and will be held from March 29 to 31, 2018. The conference will be organized by the US-based International Development Institute. More than 200 delegates including a representative from global communities of the disabled will take part in the conference that is to be held in Kathmandu and Pokhara.⁶⁴ The conference is expected to promote accessible holidays for the differently-abled and for people with physical limitations. It aims to target those who remain vastly underserved

due to inaccessible travel and tourism facilities and services. According to the Lonely Planet, the world's largest travel guide publisher, 50% of the people with disabilities would travel more if there were suitable facilities available wherever they travelled. It is expected that accessible tourism will make the tourism experience better for people of any physical condition.

Homestay promotional program launched: Marshyangdi Rural Municipality that lies in the northern part of Lamjung has launched a Homestay Scheme Promotional Program. The program has been launched to expand the emerging tourism industry into new areas and will focus on existing homestays as well. Marshyangdi Rural Municipality has launched a working plan that aims to operate at least one homestay per ward. According to Arjun Gurung, Chairman of the Marshyangdi Rural Municipality, the targeted program

will be launched in Marshyangdi, Ghanpokhara, Syurung, Chapra, Mipra and other wards.⁶⁵ Daily cultural activities are a major attraction of the homestay scheme where tourists get to look into the Nepali lifestyle. Sirubari and Ghalegaon are considered as the pioneer villages in regards to homestays. At present, there are nearly 70 homestays in Syurung, Dhagai, Chapra, Mipra and Bhusme. The Marshyangdi Rural Municipality has been conducting promotional activities to attract visitors to homestays in Ghanpokhara, which is situated at 2,250 m. Despite their efforts, homestays in Ghanpokhari have not flourished. Henceforth, the municipality will provide new operators with the necessary training and logistics to promote homestays in Ghanpokhara. The Marshyangdi Rural Municipality has allocated a budget of NPR 1 million for the initial phase of the program. The municipality will hold discussions

with new and old operators to prepare the programs.

Annapurna region receives a record number of tourist in 2017: The Annapurna region which is considered to be one of the best trekking trails in the world, welcomed a record number of tourist in 2017. According to the Annapurna Conservation Area Project, a total of 158,578 foreign tourist visited the Annapurna region in 2017, this number was 38.88% higher than the number of foreign tourist arrivals in 2016.⁶⁶ The number of trekkers was highest in October i.e. 25,300, while the number of trekkers was lowest in June i.e. 3,002. The highest number of tourists in the region were from India, followed by China, France, the UK and the USA. The other countries from which

there were high numbers of tourist arrivals were Germany, South Korea, Australia, the Netherlands and Spain. Tourists from India mostly visited the Annapurna region for religious purposes, whereas, tourists from other countries came for trekking. Tourists from the South Asian Association for Regional Cooperation (SAARC) countries sharply increased from 18,554 to 33,125 in 2016 and 2017 respectively.

Lumbini saw more than 1.55m tourists in 2017: According to the statistics of the Lumbini Development Trust, more than 1.55 million tourists visited Lumbini in 2017. The Lumbini area saw a 20.75% rise in tourists compared to the tourist numbers in 2016. Nearly 1.25 million domestic visitors

and 301,240 international tourists visited the birthplace of Gautam Buddha last year. The highest numbers of international tourists visiting Lumbini were from India, followed by Sri Lanka, Thailand and Myanmar, among others. Tourists from 87 countries visited Lumbini last year. According to one of the travel trade entrepreneurs, "Despite the growth in foreign tourist numbers, their stay in the birthplace of Buddha has not increased, nearly 90% of foreigners visiting Lumbini spend less than an hour in the area before moving on and a majority of foreign tourists visiting Lumbini are handled by Indian tour operators."⁶⁷ The country as well as the locals have not been able to reap benefits because of the limited time spent by tourists in Lumbini.

“ OUTLOOK

Nepal might finally attain the goal of "Nepal Tourism Year 2011" this year and welcome one million tourists. Despite political instability, the inflow of tourists is on a rise. The Mayors should seek help from tourism entrepreneurs and implement plans and strategies in order to support, develop and promote the tourism sector. The private sector needs to work hand in hand with local, provincial and federal governments for tourism development and promotion. The government should play a vital role in promoting homestays to decentralize tourism and boost rural economies. Important projects like upgrading the Gautam Buddha Airport in Bhairahawa to an international airport should be prioritized in order to make Lumbini a world-class tourism and pilgrimage hub.

TRADE AND DEBT

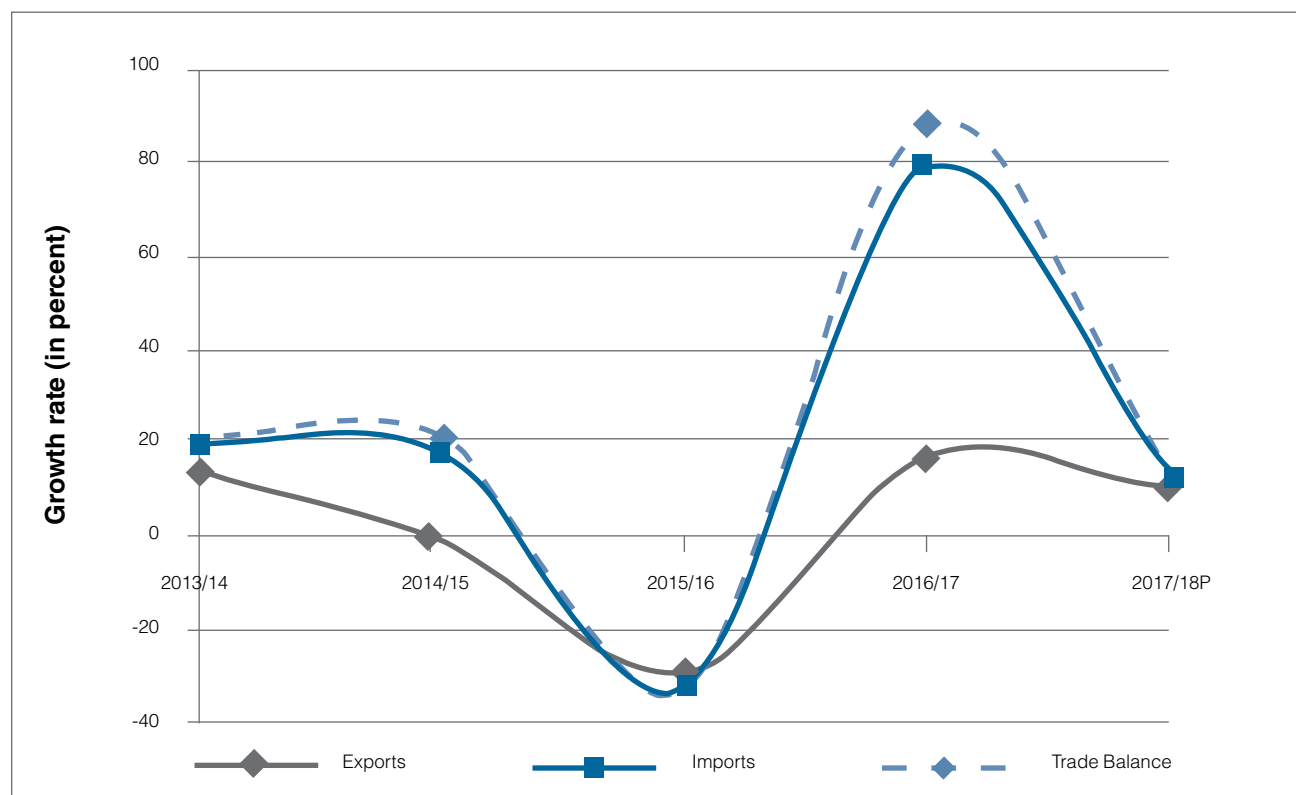
Nepal's trade deficit has been on a steady rise, alongside a slowdown in remittance growth. The first four months of Fiscal Year (FY) 2017/18 saw a marginal surplus in Balance of Payments (BOP), followed by a deficit by the end of the fifth month. Energy shortfall is the major reason behind Nepal's trade imbalance ratio, which is a little over 10:1. Despite the gloomy picture presented by the economy, the introduction of an Electronic Cargo Tracking System (ECTS) and e-commerce platform are likely to ease international trade and create a conducive trade environment in federal Nepal.

Foreign trade scenario: Table 6 shows the foreign trade scenario of Nepal based on data from the first five months of FY 2017/18. India's stringent tariff barriers in the Goods and Services Tax (GST) regime had detrimental effects on

Nepal's exports. As India increased the import tariff, Nepal's exports to India recorded a negative growth for major export items. Overall, Nepal's trade performance remained sluggish in the first five months of FY 2017/18.

In the current review period, merchandise imports to Nepal registered an increase of 12.8%, with total imports amounting to NPR 431.49 billion (USD 4.18 billion) compared to an increase of 78.9% in the same period of the previous

Figure 16: Foreign Trade Scenario during the review period for FY 2017/18.



Source: Nepal Rasta Bank Report: Current Macroeconomic Situation (based on first five month data of 2017-18)

Table 6: Foreign Trade Statistics for the first five months of FY 2017-18 (in millions)

In NPR Million	2015/16	2016/17	2017/18	Percent Change	
				2016/17	2017/18
TOTAL EXPORTS	26,169.5	30,633.2	33,695.9	17.1	10.0
To India	13,876.2	17,019.1	17,959.6	22.6	5.5
To China	479.1	744.2	1,328.0	55.3	78.4
To Other Countries	11,814.2	12,869.9	14,408.3	8.9	12.0
TOTAL IMPORTS	21,382.7	382,640.9	431,487.9	78.9	12.8
From India	121,663.4	250,362.8	283,474.9	105.8	13.2
From China	37,186.5	53,193.5	53,942.9	43.0	1.4
From Other Countries	54,977.8	79,084.6	94,070.2	43.8	18.9
TOTAL TRADE BALANCE	-187,658.2	-352,007.7	-397,792.1	87.6	13.0
With India	-107,787.2	-233,343.7	-265,515.2	116.5	13.8
With China	-36,707.4	-52,449.3	-52,614.9	42.9	0.3
With Other Countries	-43,163.6	-66,214.8	-79,661.9	53.4	20.3
TOTAL FOREIGN TRADE	239,997.2	413,274.1	465,183.8	72.2	12.6
With China	37,665.6	53,937.8	55,270.9	43.2	2.5
With Other Countries	66,792.0	91,954.5	108,478.5	37.7	18.0

Source: Nepal Rastra Bank Report: Current Macroeconomic Situation (based on first five month data of 2017-18)

year. Imports from the two adjacent neighbouring countries, India and China, witnessed an increase of 13.3% and 1.4% respectively, and that from other trading partners went up by 18.9%.

In the current review period, Nepal's merchandise exports increased by 10% to NPR 33.70 billion (USD 0.32 billion) as compared to the rise of 17.1% during the same period of last FY. Exports to India witnessed a modest rise of 5.5% as compared to Nepal's exports to China which drastically increased by 78.4%. Similarly, exports to other nations went up by 12%.

Top imports and exports: In keeping with the trend of the previous FY, increasing imports of petroleum products continued to contribute to

the overall rise in value of imports in the current review period. Petroleum products worth NPR 54408.3 million (USD 528.03 million) were imported from India, which shows that there was a 37.9% increase from the figures in the last FY. In addition, the import of raw materials required for the production of steel bars skyrocketed as post-earthquake reconstruction gathered pace. Moreover, import of vehicles, gold and polythene were among the top imports which increased by 13.1%, 36.1% and 89.3% respectively. In contrast, import of agricultural equipment, electrical goods, edible oil, sanitary ware, dry cell batteries, among others, decreased in the current review period.

The export cattle feed and zinc sheets to India went up by 408% and 18.2% compared to 124% and -13% in

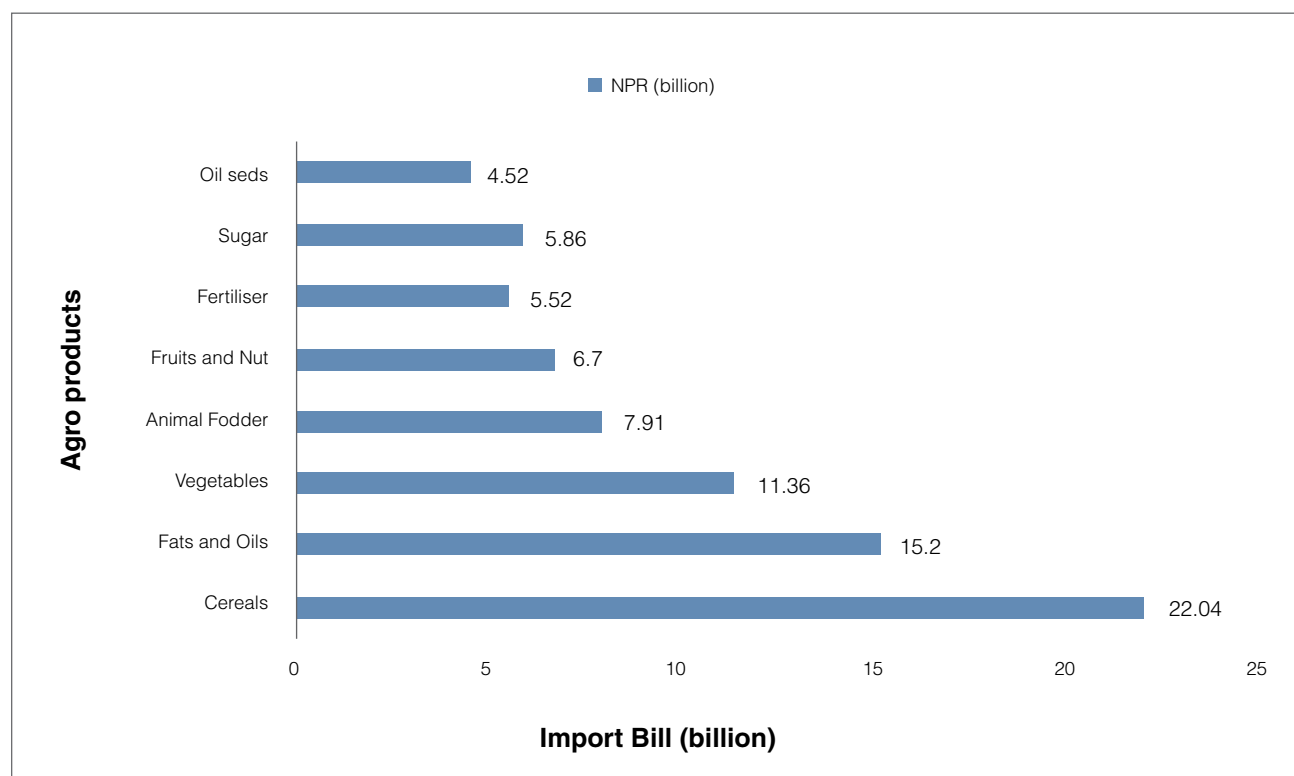
the previous FY. Commodity wise, exports of vegetable ghee, thread and readymade garments, among others, increased, whereas export of juice, cardamom, G.I. pipes, woollen carpets, copper wire rods, among others, decreased in the review period.

Trade deficit: As imports outperformed exports in the first five months of FY 2017/18, the total trade deficit widened by 13%, amounting to NPR 387.79 billion (USD 3.76 billion). As a result, the export import ratio declined to 7.8% in the review period. The country also witnessed a deficit of NPR 3.9 billion (USD 37.84 million) in the service trade after a long time, which otherwise had enjoyed surplus despite a huge deficit in goods trade.

Balance of Payments deficit: A substantial rise in the value of imports resulted in a current account deficit of NPR 41.95 billion (USD 0.40 billion) in the review period. In contrast, the current account had a surplus of NPR 3.49 billion (USD 33.87 million) in the same period of the last FY. The overall BOP documented a deficit of NPR 9.27 billion (USD 89.96 million) in contrast to a surplus of NPR 28.78 billion (USD 0.27 billion) in the same period of the last FY. Skyrocketing imports, sluggish exports, negative growth of remittance and low disbursement of foreign aid are the reasons for the huge BOP deficit of NPR 9.27 billion (USD 89.96 million), which is also the highest recorded after 2010/11.

Electronic Cargo Tracking System:

The modality of the ECTS proposed by the Ministry of Commerce (MoC) was approved by the cabinet and is expected to come into force in the near future. The ECTS will help reduce the high demurrage and detention charges incurred by Nepali importers

Figure 17: Import of agro based products during the review period, 2017-18

Source: Nepal Rastra Bank Report: Current Macroeconomic Situation (based on first five month data of 2017-18)

by controlling the turnaround time of shipping line containers.

It takes 49 days for Nepal to carry out third country trade, while it takes only 14 days for India. Shipping liners generally provide a 21-day turnaround period however; Nepali traders often miss the deadline due to delays in Indian Railways and congestion in the dry port, among other reasons.

The service will be available at USD 45 per container and it will no longer be compulsory to purchase additional insurance in India on the import of sensitive goods. The Government of India has also given a green signal to allow the movement of Nepal-bound cargoes to the nearest railhead at Jogbani after the ECTS comes into force.⁶⁸

World Bank suggests liberal trade policy: A study carried out by the World Bank Group suggested that policymakers should adopt a liberal trade policy. By doing, supply-side constraints which are a major bottleneck in promoting Nepali export can be reduced. Liberalising the trade policy will also foster productivity in Nepali industries.

Nepal's export sector has remained sluggish in the past two decades, while imports have increased. Import tariffs continue to be the dominant source of tax revenue for Nepal; they contribute 44% of the total revenue in the country. Tariff reduction on the import of raw materials and capital goods will result in short term revenue loss but will have multiplier benefits in the long run.⁶⁹

E-commerce platform to be launched: With an aim to promote products of small and medium enterprises (SMEs) in the international market, the Trade and Export Promotion Centre (TEPC) is set to launch an online e-commerce platform. The government's trade facilitating body intends to upgrade the portal into a full-fledged e-commerce platform, thereby providing a platform for SMEs to sell their products online, thus making them accessible to international buyers.

Despite the progress, SMEs will not be able to use the e-commerce platform unless the national payment gateway is built. Nepal Rastra Bank (NRB) has conducted several studies in an attempt to build the gateway.

The national payment gateway will facilitate all payment gateways such as e-sewa and other financial institutions to come under one umbrella, which will streamline processes related to online payments and settlements.

International Trade Centre (ITC), a multilateral agency under the World Trade Organisation and United Nations will support TEPC in upgrading its portal. ITC has already begun branding Nepali products

abroad, and enhancing the capacity and marketing skills of exporters by providing training on online marketing.⁷⁰

“ OUTLOOK

Nepal is increasingly integrating with the global economy, however, domestic traders have struggled to cope up with international competition, thus limiting their influence in the global market. Failure to adopt strategic policies have resulted in the slow growth of export trade for Nepal. Now with the evolution of a new federal dynamic, stronger trade policy reforms must be introduced. Bilateral trade deals are needed, as they will help reduce tariffs for Nepal and shift focus in order to address barriers to trade that are embedded in the domestic policy.

FOREIGN AID

The inflow of foreign aid in Nepal dates back to 1952 and Nepal's dependence on foreign aid has followed a steep upward trajectory ever since. Foreign aid directs Nepal's development priorities and also allows donors to pursue their objectives through a political and strategic modality. This is evident from the fact that India has made conscious efforts to mend ties with Nepal by promising an increase in foreign grants. Now, as Nepal heralds political stability through a federal system of governance, international organisations continue to provide foreign aid to fund projects related to livelihood and technical education.

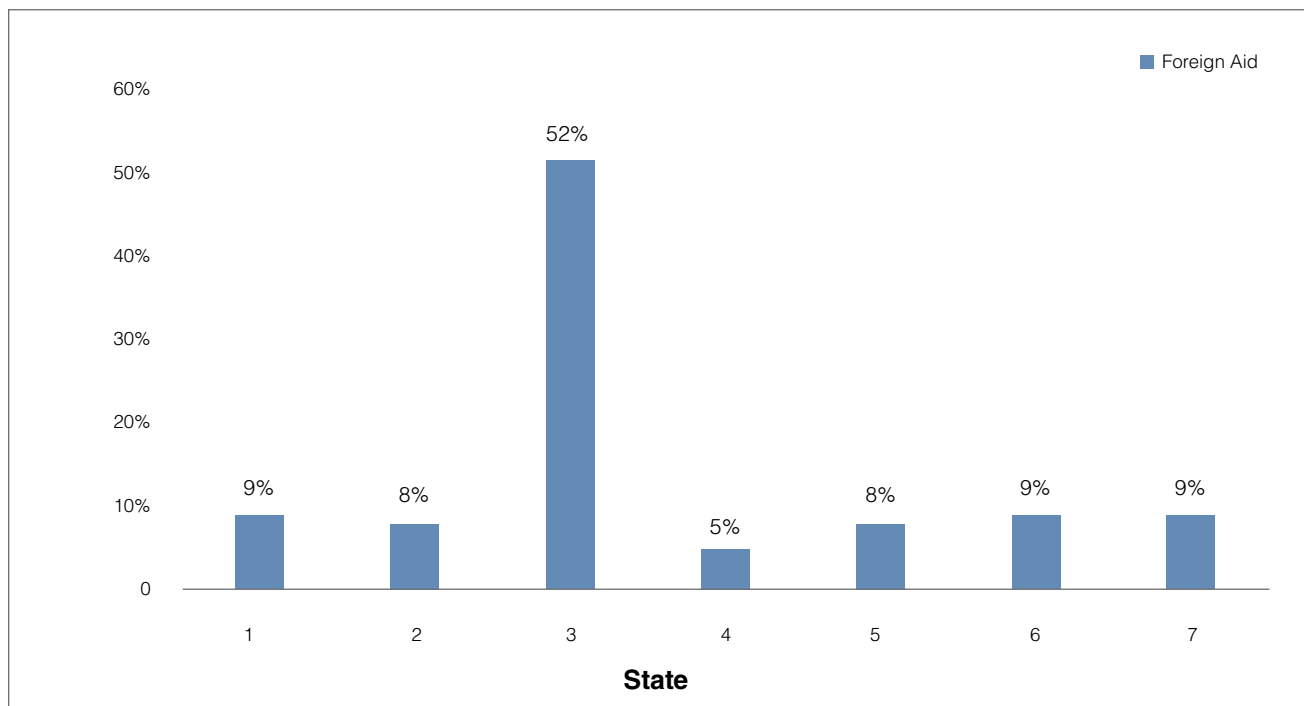
Widening inequality in foreign aid disbursement: The inflow of foreign aid in Nepal reached an all-time high in 2016, amounting to a total of USD 1394.6 billion. According to the Development Cooperation Report, 52% of the total foreign aid went to State 3 in Fiscal Year (FY) 2016/17. While, State 3 received foreign aid totalling USD 354 million,

the combined aid received by the remaining states totalled USD 323 million.

There is a yawning gap in the flow of foreign aid because it does not reflect the Human Development Index (HDI), nor is it disbursed based on geographical proximity. Instead, there is a centralised budget flow

trend that benefits just the capital city and its neighbouring districts. State 3 ranks 2nd in terms of HDI and is the top recipient of foreign aid with disbursements worth USD 354 million. In contrast, State 7 which ranks 6th in terms of HDI received USD 61.09 million worth of foreign aid. State 3 thus received five times the amount of aid that State 7 received.⁷¹

Figure 18: Foreign aid disbursement (in %) for FY 2016-17



India promises to increase grant by 74%:

India is Nepal's fourth largest bilateral donor after the US, UK and Japan. India's 2018 budget committed to increasing the financial grants to Nepal by 74% in the next FY. India pledged to grant Nepal NPR 10.6 billion (USD 0.102 billion), which will make it the second largest South Asian contributor to Nepal's foreign aid. Bhutan is the top recipient of Indian aid and will receive a grant of NPR 28.96 billion (USD 0.28 billion) in the next FY.

Of the total support received from India, NPR 118 million (USD 1.15 million) will go to the Nepal Police Academy. Major development projects supported by India such as the cross border railway line, integrated check posts, cross-border transmission lines, Arun III and Upper Karnali hydropower, Pancheshwar Multipurpose Project and the Postal Highway will benefit tremendously from the promised grant.⁷²

World Bank to provide USD 440 million credit:

The World Bank (WB) approved a concessional loan of USD 440 million to the Government of Nepal. This loan will help to aid post-earthquake reconstruction, boost innovation in the livestock sector and provide education and vocational training.

From the total of USD 440 million, USD 300 million will be allocated to the Earthquake Housing Reconstruction Project and will

rejuvenate the reconstruction process of 96,000 private houses in Nuwakot, Dhading and Dolakha. The proposed amount will also be used to make up for the financial shortfall that the government is facing in providing housing grants to beneficiaries.⁷³

USD 80 million will be allocated for the Livestock Sector Innovation Project, which will serve to bolster the role of livestock for sustained agriculture and economic growth. It will also help to achieve the objectives of the Agricultural Development Strategy (ADS) introduced by the Government of Nepal in 2015. Of the vast majority of Nepal's population engaged in agriculture, 70% raise livestock. Nearly 200,000 individuals across 271 municipalities will directly benefit from the project and at least 45% of them will be women. Furthermore, 500 small and medium sized agro enterprises will profit from production and postproduction value chains.⁷⁴

The remaining USD 60 million will finance the second phase of the Enhanced Vocational Education and Training Project, which will help strengthen the delivery of the Technical Education and Vocational Training Programme.⁷⁵

High Hill Agriculture and Livelihood Project failed:

Jointly funded by the Asian Development Bank (ADB) and the Government of Nepal, the High Hill Agriculture and Livelihood Project has failed. Over NPR 160

million (USD1.55 million) was used for this project, but no substantial progress has been made.

Out of 397 programmes registered under the project, 149 programmes received approval. Of the 149 programmes, only two goat farming programmes, one buffalo rearing programme, one dairy farming programme, and one mushroom cultivation programme are currently running. The investments made in animal husbandry sector had worse returns in comparison to those investments made in the agriculture and forestry sectors. Nearly all the dairy farms have completely shut down. Moreover, of the 86 programmes targeting animal husbandry, only one dozen farms with yaks survived.

Japan extends USD 3.15 million for food security:

Japan agreed to extend a grant worth NPR 324.8 million (USD 3.15 million) to Nepal. This grant will support the functioning of food assistance programmes in various parts of the country.

In the last FY, devastating floods and landslides hit the agriculturally productive regions of the country, causing many agricultural products to be washed away, resulting in food shortages. The grant aims to assist the Government of Nepal by implementing programmes to ensure food security for the needy. The programmes will aid in providing rice to people living in districts with food deficits.⁷⁶

“ OUTLOOK

Foreign aid continues to have a strong grip when it comes to shaping Nepal's development priorities, as more than 70% of the development projects are financed by foreign aid. However, much of the foreign aid investments in the past have clustered in and around the capital, thereby limiting their role in the overall economic development of the nation. The direction of foreign aid flow in federal Nepal will serve as a test of the effectiveness of the newly adopted federal system of governance. Having said that, innovation in aid delivery mechanisms will be crucial in achieving the desired outcomes.

REMITTANCE

The remittance inflow into the country has been hit hard by the prolonged contraction in the departure of migrant workers caused by the economic slowdown in Gulf countries and the diplomatic row in Qatar. Further negative developments such as the increase in the tax rate in Saudi Arabia and the United Arab Emirates (UAE), the regulation of working areas for expats in Saudi Arabia, and the very low minimum wage rate set in Qatar will also presumably cause the inflow of remittance to decrease further.

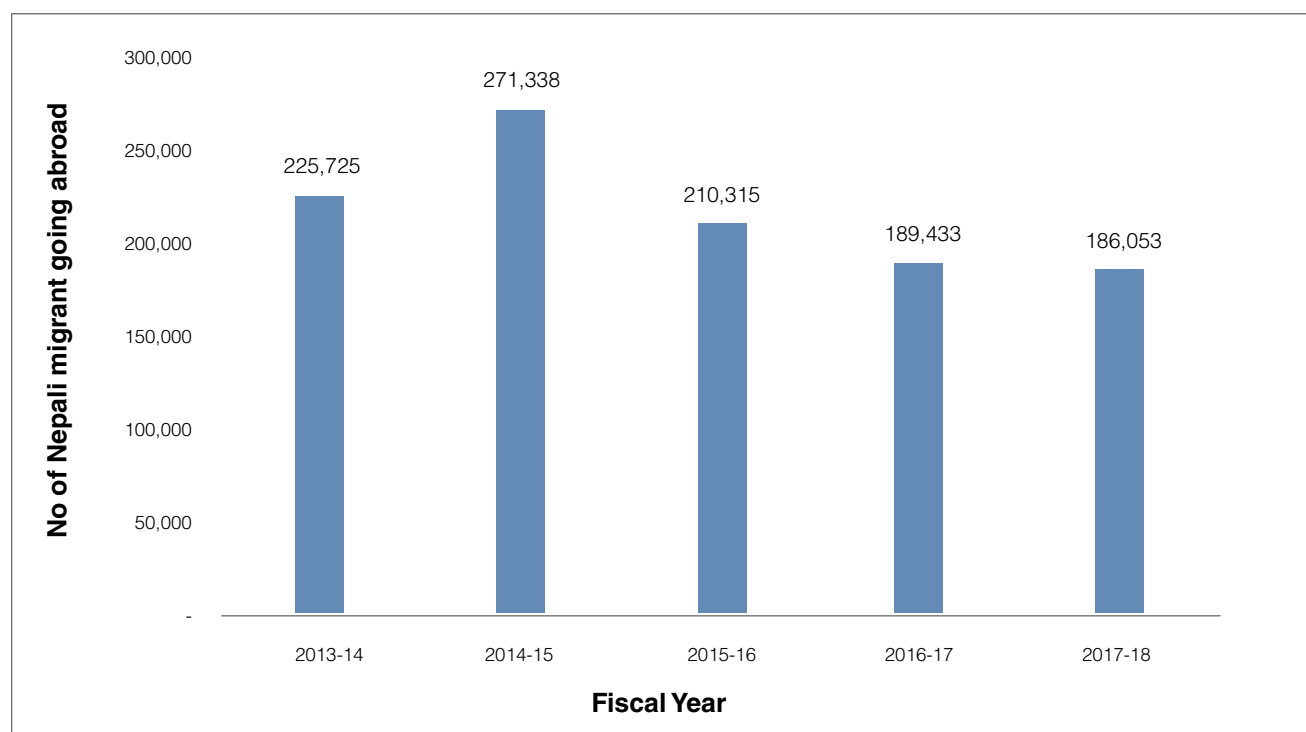
Worker's remittance decreased: Remittance inflow decreased by 0.5% to NPR 340.54 billion (USD 3.30 billion) in the first six months of Fiscal Year (FY) 2017/18 as compared to the 5.7% growth it underwent in the corresponding period of the previous year. Remittance has been declining from the second half of the FY 2015/16. The number of job seekers

for foreign employment decreased by 1.8% to 186,053 from 189,433 in the review period. This decrease was 9.9% in the corresponding period of the previous year.

Decrease in foreign labour migrants: The number of Nepali migrants going abroad for foreign employment declined by 4% in the first six months

of the ongoing FY i.e. FY 2017/18 as compared to FY 2016/17. As per the Department of Foreign Employment (DoFE), in the first six months of the FY, a total of 174,158 Nepalis obtained work permits for the four most preferred foreign labour destinations, i.e. Malaysia, Qatar, Saudi Arabia, and the UAE. During the same period in the corresponding year, the

Figure 19: Outflow of Nepali migrant workers for Foreign Employment in first six month of FY 2017/18



Source: Current Macroeconomic and Financial Situation (Based on Five Month's Data of 2017/18, Nepal Rastra Bank)

number of workers that obtained work permits for the same four destinations was 184,053. As per the statistics, Malaysia has superseded Qatar and Saudi Arabia as the most preferred destination for Nepali workers. The number of workers going to Malaysia increased by 19,317 to 58,659 in the first six months of the FY 2017/18, whereas Nepali workers going to Saudi Arabia and Qatar decreased by 21,201 and 14,007 to 43,566 and 45,115 respectively (refer to Figure 20).⁷⁷

Remittance likely to be hit by the UAE and Saudi Arabia's plan to introduce VAT: Saudi Arabia and the UAE plan to impose a 5% tax on goods and services starting from the next FY. By doing so, they aim to boost revenue. Similarly, other Gulf countries are also expected to revise their VAT schemes in the coming years. This

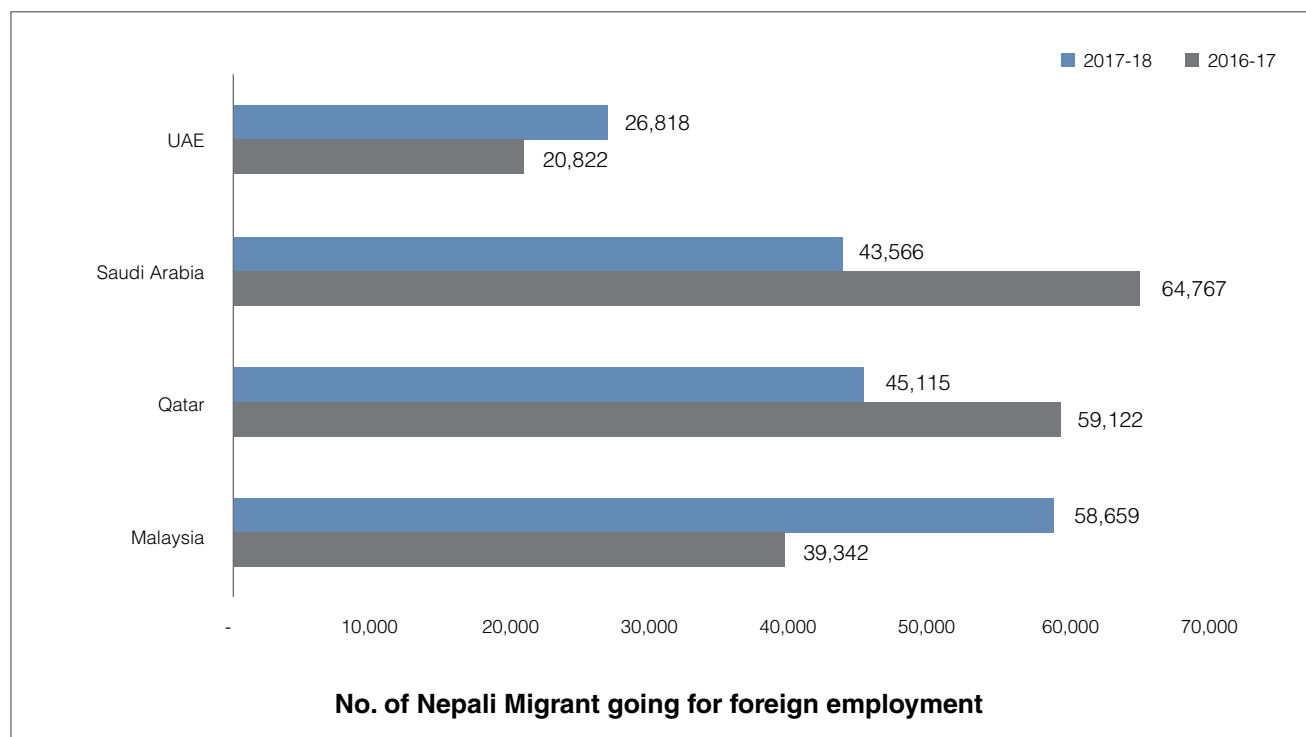
imposition of new tax regulations is expected to cause a domino effect as savings would decrease due to the increase in the cost of living, thereby further curtailing the remittance inflow. In this context, the Chairman of Nepal Association of Foreign Employment Agencies (NAFEA) Rohan Gurung urged the government to make substantial diplomatic efforts to address imminent issues.⁷⁸

Saudi Arabia restricts expats from working in certain sectors: In January 2018, Saudi Arabia issued a ministerial decision to reserve jobs exclusively for its citizens in 12 working areas. The decision will be implemented starting in September 2018. This decision has been considered as a major setback for the Nepali labour market as Saudi Arabia is a preferred labour

destination for Nepali migrants. The restricted working areas include electrical and electronic shops, outlets selling spare car parts, shops that sell building materials, and shops that sell home furniture and ready-made office material. The Chairman of NAFEA Rohan Gurung claims that the decision could have a substantial impact on remittance in Nepal, as it will particularly affect the migration of skilled workers.⁷⁹

Qatar sets minimum basic wage rate that is less than Nepal's provision: Qatar has set the minimum wage for workers at 750 Riyals (USD 202.5) per month. This is 150 Riyals (USD 40.5) less than what Nepal has provisioned for minimum wage for its citizen working in Gulf countries as unskilled workers. As per the new

Figure 20: Figure showing number of Nepal migrant going to top four labour destinations



provision, Qatari companies will not be paying more than 750 Riyals (USD 202.5) to migrant workers. The new wage rule introduced by Qatar is likely to cause a decrease in the income of Nepali workers and increase their financial burden. However, the government of Nepal is choosing to stick with its own minimum wage provision. Such an intractable stance on the part of the Nepali government could promote the practice of fake contracting or paperwork and diminish the demand of Nepali workers.⁸⁰

“ OUTLOOK

The excessive dependency of the country's economy on remittance gives cause for concern, especially considering the continuous decline in the inflow of remittance. The hostile working environment of the host countries (for Nepali workers) has made the situation bleaker. Therefore, it is entirely plausible that if the government does not take proactive steps and implement proper strategies, macroeconomic disequilibrium such as a balance of payment deficit, a liquidity crunch and further widening of the trade-deficit could be triggered.



MARKET
REVIEW

FINANCIAL MARKET

The financial performance of commercial banks is starting to reflect the effect of a liquidity crisis. The average cost of funds of commercial banks has risen to 3.8% as compared to 2.7% during the same period in the last fiscal year (FY), while the average base rate of commercial banks has gone up to 9.9%.

Key Indicators

Some of the key macroeconomic indicators as per the macroeconomic and financial situation report based on the first six months of FY 2017/18 published by Nepal Rastra Bank (NRB) are highlighted below.

Deposit and Credit Mobilisation

Deposits at Banks and Financial Institutions (BFIs) increased by 6.9% in the review period. Of the total deposits at BFIs, the share of demand deposits and fixed deposits increased by 8.4% and 42.8% respectively while the share of saving deposits decreased from 42.1% to 36.4% in mid-January 2018.

Likewise, credit extended to the private sector by BFIs increased by 11.9% in the review year as compared to an increase of 12.9% in the previous FY. Credit mobilization of commercial banks, development banks and finance companies increased by 11.5%, 16.6% and 4.2% respectively. Of the total outstanding credit of BFIs, 61.3% is against the collateral of land and building and 14.5% against the collateral of current assets such as agricultural and non-agricultural products.

In terms of credit exposure, the outstanding credit of BFIs to real estate loan increased by 9.5% and trust receipt loan extended by commercial bank increased by 50.5% during the year. Similarly, Hire Purchase loan increased by 7.0% while overdraft loan increased by 9.6%.

Liquidity Management

In the review year, NRB mopped up liquidity of NPR 129.20 billion (USD 1.25 billion) in the banking system through various open market operations such as deposit collection auction worth NPR 42.35 billion (USD 411.01 million) and reverse repo auction worth NPR 84.75 billion (USD 822.49 million). Likewise, BFIs used Standing Liquidity Facility (SLF) worth NPR 23.58 billion (USD 228.84 million) during the review period. Moreover, NRB injected net liquidity of NPR 198.04 billion (USD 1.92 billion) through the net purchase of USD 1.92 billion from foreign exchange market (commercial banks).

Similarly, NRB also purchased Indian currency (INR) equivalent to NPR 231.64 billion (USD 2.25 billion) through the sale of USD 2.20 billion and Euro 40 million during the review year. INR equivalent to NPR 224.30 billion (USD 2.18 billion) was

purchased through the sale of USD 1.98 billion and Euro 95 million in the previous year.

Foreign Exchange Reserves and Adequacy

The gross foreign reserves stood at NPR 1067.34 billion (USD 10.35 billion) at the end of mid-January 2018, decrease of 1.1% compared to NPR 1,079.43 billion (USD 10.48 billion) in mid-July 2017. Out of the total foreign exchanges, reserves held by NRB increased by 0.7% to NPR 933.82 billion (USD 9.06 billion) at mid-January 2018 from NPR 927.27 billion (USD 8.99 billion) as at mid-July 2017. The share of INR in total reserves stood at 23.9% as at mid-January 2018.

Based on the imports of FY 2017/18, the foreign exchange holdings of the banking sector is sufficient to cover the prospective merchandise imports of 12.2 months, and merchandise and services imports of 10.6 months. The ratio of foreign currency reserve-to-GDP, reserve-to-imports and reserve-to-M2 stood at 41.1%, 87.9 % and 38.6 % respectively as at mid-January 2018.

Interest Rates

The weighted average 91-day Treasury bill rate increased to 5.82% in the

review period from 1.74% a year ago. Likewise, the weighted average inter-bank transaction rate among commercial banks also increased to 4.40% from 2.71% a year ago. Also, the weighted average base rate of commercial banks increased to 9.94% from 7.1% a year ago.

Balance of Payments (BOP)

In terms of BOP, the current account fell into a deficit by NPR 75.71 billion (USD 734.76 million) during the review period as compared to a deficit of NPR 1.08 billion (USD 10.48 million). Nonetheless, the overall BOP posted a deficit of NPR 6.66 billion (USD 64.64 million) in the review year compared to a surplus of NPR 45 billion (USD 436.72 million) in the same period of previous year.

In the review period, Nepal received Capital transfer of NPR 10.07 billion (USD 97.73 million) and Foreign Direct Investment (FDI) inflow of NPR 14.33 billion (USD 139.07 million) compared to transfer of NPR 7.93 billion (USD 76.96 million) and inflow of NPR 7.39 billion (USD 71.72 million) respectively in the same period of the previous year.

Second Quarter Performance Analysis of Commercial Banks

As per the unaudited second quarter financial results of commercial banks for FY 2017/18 as shown in Table , the operating profit of commercial banks grew by 10.4% while the net profit increased by 10.2% compared to the corresponding figure of the previous FY.

Nabil Bank was able to post the highest net profit of NPR 1.84 billion (USD 13.29 Million), followed by Nepal Investment bank at NPR 1.83 billion (USD 9.34 million) and Rastriya Banijya Bank at NPR 1.78 billion (USD 8.57 million) at the end

of this quarter. During the review year, the deposit mobilisation increased by 15.7% while credit mobilisation by the commercial banks increased by 20.7%.

At the end of the second quarter, the average Non-Performing Loan (NPL) of banks had increased to 1.7% from 1.6% as compared to the corresponding period, and the average cost of funds of commercial banks increased to 6.4% from 3.8%. Similarly, the average base rate of commercial banks stood at 9.9% during the end of this quarter, the highest being 11.5% of the Agricultural Development Bank, Civil Bank and NCC Bank, and the lowest being 5.8% of Standard Chartered Bank.

Key Developments Fresh Directives/Circulars from Nepal Rastra Bank

- **Cooling period of Chief Executive and Board Members:** With an objective of curbing unhealthy practices and strengthening corporate governance in the banking sector, the central bank has issued a circular to introduce a cooling period of six months for chief executives of BFIs. From now onwards, the chief executive of any BFI can join another BFI only after six months of quitting the previous BFI. Similarly, the cooling period will also be in place for a chief executive who seeks to re-join the same BFI, irrespective of the reasons for quitting the institution. Moreover, the same rule applies for the Board of Directors of BFIs as well. However, such a rule will not be applicable to professional or independent directors.
- **Risk Management Directive:** NRB has made it mandatory for

BFIs to appoint a chief risk officer in order to formulate strategies to identify and manage risks, and introduce a credit rating system. This will help evaluate the worthiness of borrowers, thereby making it easier to manage risks in the financial market. With the enforcement of the new directive, there have been two new additions to the banking sector's risk categories. These additions are market and other risks, in addition to the existing risk categories such as credit and investment, operational, interest rate, liquidity and foreign exchange. Further, the regulator has made the Board of Directors of BFIs fully responsible for risk management and has also made it mandatory for commercial and development banks to develop a credit rating system to evaluate credit worthiness of borrowers.

- **Permission to receive foreign award:** NRB has made it mandatory for BFIs to seek permission before accepting awards from any foreign agencies. The legitimacy and credibility of foreign entities must be established before documents are presented to the NRB and before the BFIs accept the award. NRB also imposed a compulsion for BFIs to implement a guideline on foreign trips undertaken by chairmen, CEOs and board members of BFIs within mid-April. The guideline will authorise the board of directors to sanction foreign trips upon the assessment of the benefits that BFIs will derive from the foreign visits.⁸¹

Mid-year review of Monetary Policy

The central bank came out with a half yearly review of its monetary policy for the FY 2017/18. The mid-term

TABLE 7: SECOND QUARTER RESULTS OF COMMERCIAL BANKS-UNAUDITED-AS ON FY 2017-18 (FIGURES IN NPR TEN MILLION)

Bank	Paid-up Capital		Reserve & Surplus	DEPOSIT			LOANS AND ADVANCES			OPERATING PROFIT			NET PROFIT			NPL (%)			COST OF FUND (LCY)			BASE RATE (%)	
	FY 17/18	FY 16/17		% Change	FY 17/18	FY 16/17	% Change	FY 17/18	FY 16/17	% Change	FY 17/18	FY 16/17	% Change	FY 17/18	FY 16/17	% Change	FY 17/18	FY 16/17	% Change	FY 17/18	FY 16/17		% Change
Nabil Bank	804.3	785.5	12,128.9	12,081.3	0.4	10,085.1	9,030.0	11.7	273.9	262.8	4.2	183.7	174.7	5.2	1.1	0.9	4.4	4.4	1.9	2.5	6.9		
Nepal Investment Bank	1,062.6	991.1	12,984.5	11,660.7	11.4	11,367.1	9,670.9	17.5	244.6	232.4	5.2	183.0	158.4	15.5	1.1	0.7	6.2	6.2	3.5	2.7	9.0		
Standard Chartered Bank	801.1	486.6	6,607.2	6,198.6	6.6	4,235.9	3,510.6	20.7	155.3	112.0	38.7	101.3	74.0	36.9	0.2	0.3	2.4	2.4	1.3	1.1	5.8		
Himalayan Bank	811.4	469.6	9,297.2	9,109.8	2.1	8,275.7	7,556.7	9.5	140.4	160.9	(12.7)	110.5	102.7	7.6	1.3	0.9	6.4	6.4	2.7	3.7	9.4		
Nepal SBI Bank	804.6	369.2	8,516.9	7,759.9	9.8	7,134.1	5,977.2	19.4	143.5	116.4	23.3	91.3	75.8	20.4	0.1	0.1	5.1	5.1	2.5	2.6	9.5		
Nepal Bangladesh Bank	808.5	279.1	4,189.0	4,103.7	2.1	4,111.3	3,620.1	13.6	63.0	74.0	(14.9)	43.8	54.0	(18.9)	1.5	1.0	7.9	7.9	4.4	3.5	11.4		
Everest Bank	810.6	519.0	10,329.9	9,043.6	14.2	8,473.6	7,261.8	16.7	177.5	148.6	19.4	114.0	97.1	17.4	0.3	0.7	5.0	5.0	2.8	2.8	7.8		
Bank of Kathmandu Lumbini	624.5	489.7	7,043.9	7,000.0	0.6	6,466.9	6,278.8	3.0	75.6	86.5	(12.6)	55.1	60.1	(8.3)	1.9	1.5	7.6	7.6	4.2	3.5	10.4		
NGC Bank	467.9	291.4	5,891.3	5,546.8	6.2	5,141.8	4,842.2	6.2	17.4	7.6	128.9	35.4	7.7	359.7	4.0	4.8	8.2	8.2	5.3	2.9	11.5		
NIC Asia Bank	803.1	265.5	12,046.6	7,907.1	52.4	10,220.0	6,749.5	51.4	76.3	76.4	(0.0)	57.2	72.1	(20.7)	0.3	0.7	7.6	7.6	4.5	3.1	10.8		
Machhapuchhre Bank	805.5	144.9	6,579.8	5,824.0	13.0	6,026.5	5,185.3	16.2	68.6	84.9	(19.2)	47.1	57.5	(18.1)	0.3	0.4	7.6	7.6	3.8	3.8	10.7		
Kumari Bank	596.9	259.0	5,768.0	3,994.6	44.4	5,092.4	3,365.9	51.3	34.5	35.9	(3.9)	48.0	27.9	72.0	1.6	1.1	7.8	7.8	4.7	3.1	11.2		
Laxmi Bank	822.1	188.6	6,027.9	5,555.4	8.5	5,502.2	4,671.0	17.8	69.0	48.9	41.1	51.9	40.6	27.8	1.3	1.3	7.4	7.4	5.3	2.2	10.9		
Siddhartha Bank	705.6	410.4	8,556.6	7,493.5	14.2	7,569.5	6,265.9	20.8	86.6	87.1	(0.6)	77.2	72.6	6.3	1.5	1.5	7.3	7.3	4.2	3.1	10.6		
Global IME Bank	888.8	336.9	10,021.6	8,412.6	19.1	8,809.4	7,151.6	23.2	117.1	117.6	(0.4)	95.2	90.6	5.1	1.6	1.6	7.0	7.0	4.1	2.9	10.3		
Citizens Bank International	802.9	199.6	5,846.4	5,274.9	10.8	5,331.6	4,678.2	14.0	117.1	68.2	71.7	62.8	63.1	(0.5)	1.9	1.3	8.2	8.2	5.2	3.0	11.0		
Prime Commercial Bank	803.3	211.6	7,106.0	5,500.6	29.2	6,260.1	4,605.2	35.9	94.4	73.4	28.6	71.5	55.9	27.9	1.4	1.4	8.2	8.2	4.5	3.7	10.8		
Sunrise Bank	815.2	210.0	6,326.9	5,730.0	10.4	5,624.1	4,922.3	14.3	83.0	82.0	1.2	58.7	60.9	(3.6)	1.7	1.4	7.3	7.3	4.6	2.7	11.0		
NMB Bank	646.1	523.2	8,055.2	6,879.7	17.1	7,093.1	6,040.4	17.4	113.6	82.0	38.5	100.7	70.1	43.7	1.2	1.9	7.1	7.1	4.0	3.0	10.4		
Prabhu Bank	653.3	310.7	8,612.8	7,021.6	22.7	7,163.7	5,652.9	26.7	59.5	93.4	(36.3)	63.4	111.2	(43.0)	4.1	4.9	-	-	-	-	9.7		
Janata Bank Nepal	800.0	106.6	5,280.1	2,556.4	106.5	4,869.1	2,297.8	111.9	22.6	15.9	42.1	22.1	16.1	37.3	2.7	2.6	7.8	7.8	4.6	3.3	11.4		
Mega Bank	737.6	167.6	4,557.3	3,851.7	18.3	4,076.7	3,401.1	19.9	47.3	52.7	(10.2)	39.3	37.0	6.2	1.0	0.7	7.6	7.6	4.5	3.1	11.0		
Civil Bank	518.5	173.9	3,700.8	3,293.4	12.4	3,355.3	2,950.5	13.7	3.55	0.20	1,675.0	21.6	16.7	29.3	4.5	4.5	8.1	8.1	5.6	2.6	11.5		
Century Commercial Bank	767.9	176.0	5,217.7	3,267.5	59.7	4,702.4	2,901.6	62.1	39.2	32.7	19.9	32.5	22.3	45.7	1.0	0.5	8.3	8.3	5.4	3.0	11.4		
Sanima Bank	800.1	188.4	6,839.9	5,179.1	32.1	6,052.0	4,692.1	29.0	124.6	95.3	30.7	82.4	62.2	32.5	0.0	0.0	7.2	7.2	4.1	3.2	9.7		
Public Sector Banks																							
Nepal Bank	80.4	504.7	9,189.8	8,483.3	8.3	7,871.0	7,081.5	11.1	177.9	138.3	28.6	163.8	189.5	(13.6)	3.2	2.9	2.9	2.9	2.0	1.0	6.9		
Rastriya Banijya Bank	858.8	367.8	14,910.4	13,829.6	7.8	11,065.4	9,990.6	17.8	203.8	115.5	76.5	178.5	121.7	46.7	3.1	2.8	2.0	2.0	1.3	0.8	6.0		
Agriculture Dev. Bank	1,393.7	850.5	9,817.3	8,765.9	12.0	9,211.2	8,705.7	5.8	41.0	68.4	(40.1)	102.9	90.6	13.6	4.0	3.8	7.2	7.2	4.8	2.4	11.5		
Total	21,295.3	10,277.1	221,449.9	191,325.3	15.7	191,187.2	158,457.4	20.7	2,870.9	2,570.0	11.7	2,294.9	2,083.1	10.2	1.7	1.6	6.4	6.4	3.8	2.7	9.9		

review of monetary policy signals that the status of economy to be mixed as economic activities has increased due to successful completion of local, state and federal election, uninterrupted supply of electricity and rise in tourists. Nonetheless, rise in capital account deficit and mismatch of resource mobilization seen in the banking sector poses imminent challenges to economic and financial stability. Some of the key highlights, revisions and provisions outlined by the mid-year review of the monetary policy are as follows:

- To expedite opening up of branches in all the 753 local bodies, commercial banks who have committed to open branches in local bodies should establish branches in areas where minimum infrastructure is available, within the end of the current FY 2017/18. Moreover, only those commercial banks would be able to establish branches in Kathmandu and Lalitpur Metropolitan area that establishes two branch offices in 109 local bodies that are yet to

receive any commitments from commercial banks to open bank branch.

- To control misuse of lending via overdraft loan facility, Banks having overdraft loan portfolio of more than 15% would have to decrease the portfolio size under the cap of up to 15% by the end of mid-January 2019.
- BFIs would be fined if the monthly average of their credit to core-capital-cum-deposit (CCD) ratio exceeds the regulatory limit. Currently, BFIs that breach CCD ratio are being fined every day.
- Banks and financial institutions that fail to disburse 25% loan to the productive sector i.e. 10% of total loans to agricultural sector, 5% to energy sector, 5% to tourism sector and another 5% to other priority sectors within the deadline of mid-July 2018 can buy loan from another bank that has exceeded the given target.

Table 8: Status of Key Monetary Indicators as of Mid-January, 2018

	Target/Objectives of Monetary Policy 2017/18	As on Mid-January 2018
Broad money supply (M2) growth rate	18%	14%
Domestic credit growth	27.8%	21.7%
Private sector credit growth	20.0%	17.3%
Productive sector lending	25%	22.6%

Source: Nepal Rastra Bank

Table 9: Presence of commercial banks at local level

State	Local Bodies	Presence of commercial banks
1	137	65
2	136	60
3	119	66
4	77	38
5	133	75
6	63	17
7	88	31
Total	753	352

Source: Nepal Rastra Bank

“ OUTLOOK

Compared with the first quarter results of the current Fiscal Year 2017/18, commercial banks performed better at the end of second quarter. The operating profit which saw a meagre growth of 0.8% during the last quarter saw a promising growth of 10.4% during the second quarter. Likewise, the net profit which saw a negative growth of 3.8% rebounded with a positive growth rate of 10.2%.

Despite pro-active usage of open market operations for timely liquidity injections by the regulator, the banking system is still struggling to restore balance between deposit and credit growth. The brunt of such mismatch has been easily transferred to end consumers as BFIs continue to book handsome profits. Nonetheless, the fate of liquidity yet again remains on the capacity of the government to expedite its capital expenditure amidst decline of remittances from abroad.

The expansion of physical branches of BFIs is expected to expedite in the coming days. The government has made it mandatory to have at least one physical branch of BFIs in each local level body. Moreover, the central bank via the mid-year monetary policy has clearly mandated banks to open up branches in those local bodies having minimum infrastructure availability within the end of the current Fiscal Year. As per NRB's latest figures, out of 753 local bodies, commercial banks physical branches are present in only 352 local bodies. State 5 (56 %) has the highest presence of commercial banks while State 6 (27%) has the lowest presence. Lack of security along with unavailability of basic facilities such as; electricity, internet and adequate road network are some of the challenges faced by BFIs to open branches in rural locations.

CAPITAL MARKET

The secondary market went down by 6.85% to close at 1391.03 points during the review period (November 23, 2017 to February 9, 2018) as selling pressure continued amidst tight liquidity in the banking sector.

Secondary market

During the review period, the Nepal Stock Exchange (NEPSE) benchmark index decreased by 6.85% (102.26 points) to close below long-term support of 1400 points at 1391.03 points. At the end of the review period, the total market capitalisation had reached

NPR 1,626 billion (USD 15.78 billion) while the total floated market capitalisation was NPR 547 billion (USD 5.3 billion).

As shown in Table 10, during the review period, all the sub-indices ended in the red zone. The insurance sub-index (-11.46%)

was the biggest loser as selling pressure mounted in the market. This was followed by the sub-index development bank (-10.26%) and other (-8.81%).

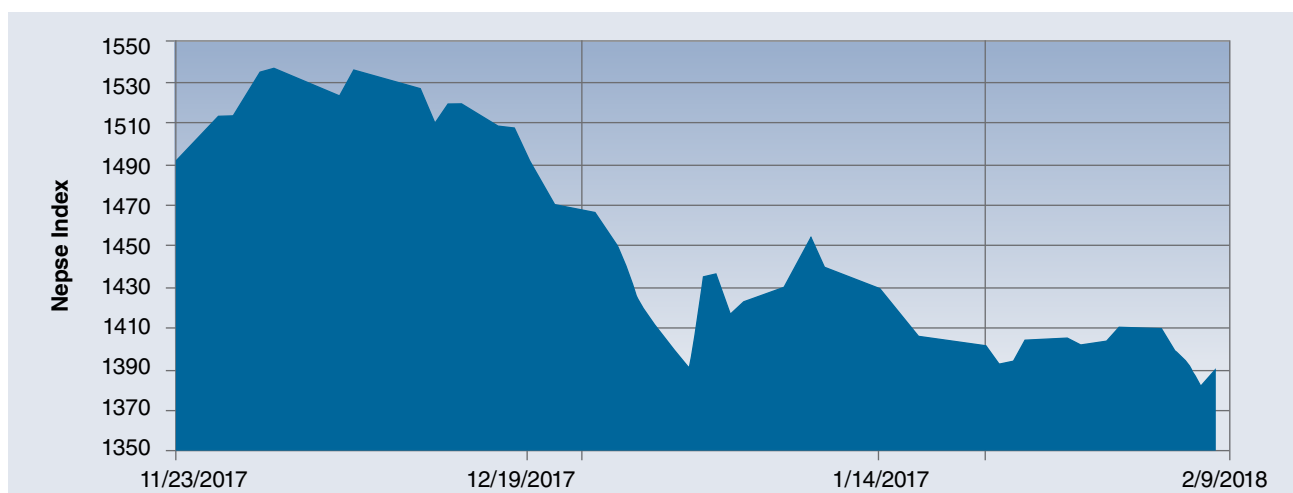
The total market turnover during the review period was NPR 269 billion (USD 2.61 billion).

Table 10: Key Indicators

Indicators	17 Aug-17	23 Nov-17	% change
NEPSE Index	1493.29	1391.03	-6.85%
Commercial Bank Index	1280.18	1212.05	-5.32%
Development Bank Index	1752.80	1572.31	-10.29%
Finance Index	753.47	707.78	-6.06%
Insurance Index	7981.09	7066.46	-11.46%
Hydropower Index	1922.14	1780.32	-7.38%
Manufacturing & Processing Index	2477.69	2450.48	-1.09%
Micro-Finance Index		1661.72	
Hotel Index	2102.36	2083.85	-0.88%
Others Index	835.24	761.65	-8.81%

Source: NEPSE

Figure 21: NEPSE Movement Index



Source: NEPSE

Primary Market

On the public issue front, the market witnessed Initial Public Offerings (IPOs) and Further Public Offering (FPO) of numerous companies and schemes during the review period.

- Unnati Microfinance issued IPO of 165,000 units worth NPR 16.5 million (USD 160,000). ICRA Nepal has assigned a Grade 4 rating to this IPO, indicating below average fundamentals of the company.
- The NIC Asia Growth Fund floated 100 million unit shares worth NPR 1 billion at par value of NPR 10 per unit. ICRA Nepal had assigned AMC Quality 3, indicating adequate credit quality ratings on management quality.
- Citizen Mutual Fund-1 issued a 7 year closed end fund of 100 million unit shares worth NPR 1 billion at par value of NPR 10 per unit.
- Premier Insurance Company (Nepal) issued FPO of 659,565 units worth NPR 526.9 million at NPR 799 per unit. The total collection of FPO was around NPR 3.22 billion. ICRA Nepal had assigned Grade 3+ to the FPO indicating average fundamentals.
- Butwal Power Company Limited (BPCL) issued Further Public Offering (FPO) of 4.08 million unit. After the FPO, its paid up capital will reach NPR 2.21 billion (USD 21.4 million). BPCL aims to use the amount collected from the FPO to develop the 37.6 MW Kabeli-A Hydropower Project and the 30 MW Nagdi Hydropower project.

Key Developments

Nepal Rastra Bank to offload its stake from NEPSE

Nepal Rastra Bank (NRB), the central bank, has decided to offload its stake from the Nepal Stock Exchange

(NEPSE), which is the sole secondary market of the country. NRB currently holds a 34.6% stake in NEPSE. The central bank plans to offload its shares through the auction model. The central bank had initially announced that it would offload its stake from NEPSE five years ago. However, the plan was mentioned in the monetary policy only in the current Fiscal Year (FY). Moreover, NRB also plans to offload its stake from Rastriya Beema Sansthan, Rural Microfinance Development Centre and Nepal Grameen Bikas Bank.⁸²

Listed Companies Corporate Governance Directives 2017

To further strengthen good governance and financial discipline, the Securities Board of Nepal (SEBON) has issued “Corporate Governance Code for listed companies”. Some of the highlights of the fresh directive are;

- Board member of the listed company can serve for a maximum of four years.
- An individual cannot hold the position of both Chairperson and Chief Executive of the listed company

- The Board member of listed companies are forbidden from working in any other organisation during his tenure as an; employee, auditor, advisor, executive, insurance surveyor, insurance broker, insurance underwriter or third-party facilitator.
- Listed companies need to make public their financial information on a regular basis.

Additional requirement for hydropower companies

In a bid to minimise anomalies and increase transparency, SEBON has directed all aspiring hydropower companies planning to go public to publish a public notice regarding their net worth and earnings per share (EPS) according to their latest audited report before issuing an IPO. Further, the regulator has directed that companies publish other key relevant information such as per megawatt production cost, assumption of time to complete the project and the payback period. Moreover, from now onwards, the hydropower companies will have to submit their annual financial report to SEBON.

“ OUTLOOK

Despite the successful completion of both provincial (state) and federal elections, the delay in the formation of new leadership has demolished investors' confidence, as the political transition has created unnecessary uncertainty. Moreover, tight liquidity in the banking sector has further affected the market. Higher returns on bank savings which provides safe returns are attracting investors, while investors who have borrowed from banks and financial institutions (BFIs) to invest in the secondary market are selling off their holdings to repay their loans due to higher interest on such loans. Further, the under subscription of the latest public offering of two mutual funds and one hydro company indicates the level of liquidity and lower investors' confidence.

Besides the tight liquidity, many investors seems to be selling off their bonus and rights shares to book profit, which has further mounted selling pressure in the market. Moreover, the charm of investors' towards BFI stocks are also fading away, as BFIs have fulfilled their increased paid-up capital which earlier were announcing frequent bonuses and the right issues to meet the stipulated requirements. The market may continue with its existing trend with some downtrend retracements as the liquidity in the banking sector continues to tighten.



**DOING BUSINESS IN
FEDERATED NEPAL**

INDIA'S FISCAL FEDERALISM AND SOME LESSONS FOR NEPAL

Rajeev Malhotra, Professor and Executive Director at Center for Development and Finance,
Jindal School of Government and Public Policy, India

India would not have been what it is today, a democratic nation that has been reasonably successful in resolving the inherent contradictions in the path of its nationhood, managing the diverse competing claims and aspirations of its people and creating a process for sustained development of the country, but for the system of fiscal federalism that its founding fathers created for the nation at the time of its independence. A religious, linguistic, racial and socially diverse group of people and the regions that they inhabited were brought together to form a nation based on a Constitutional demarcation of roles and responsibilities between the government at the union or central level and the provincial and state level. A third tier of local self-governments, both in urban and rural areas were added formally to the arrangement of fiscal relations with the 73rd and 74th Constitutional amendments in 1992, thus creating a truly multi-level fiscal system in the country. In order to inform the relationship between the different tiers of government that is further influenced by the evolving contexts and needs of the people and their regions, a statutory mechanism in the form of a Finance Commission has been constituted every five years to assess and recommend changes that are required for the system to work effectively and efficiently.

A major challenge of fiscal relations in a federated entity is to address the problem of vertical imbalance that arises on account of efficiency considerations that require all broad-based taxes to be collected by the national entity, and major public expenditure functions getting assigned to the provincial/state and sub-state governments. To address this imbalance in the assigned roles and (financial and other) capacities between different tiers of government, there has to be a mechanism to transfer resources from the national to the sub-national levels. The objective of ensuring horizontal equity, across regions and people within regions, guides this mechanism of resource transfers in a federated system. Such a mechanism is at the core of fiscal federalism in India and the system has worked well

with the periodic assessments and recommendations of the Finance Commission that take care of the changing needs and aspirations of the entities in the country. Further, for an optimal fiscal system in a federated entity, the economic stabilisation and redistribution functions must rest with the national government, and allocative functions (for the supply of public goods) with the sub-national governments. Both levels of government must have capacities at their command to deliver on their assigned responsibilities.

Although fiscal federalism as practiced in India has stood the test of time and delivered on its substantive promises, there are areas where the process underpinning the system could have been better managed and resourced, with a view to support more inclusive outcomes, sensitivity in meeting local needs and aspirations, and with better accountability of the public delivery process. There are therefore some important takeaways for Nepal from the working of India's fiscal federalism.

First, unlike India, Nepal must not undermine the government at the local level because of the apparent need to create a strong system of governance at the provincial level. In other words, politics at the provincial/state level should not be allowed to weaken the capacity of the local government, both in urban and rural areas, to deliver public goods and services in a contextually appropriate and accountable manner. This requires transfer of functions, functionaries and funds, in adequate measures, to the third tier of government so it can build its capacity. In India, despite the relevant Constitutional provisions that have been in place now for over two decades, the local governments are practically at the mercy of the provincial/state governments and the politics playing out at that level. Because of this, the emergence of a competitive and contextually appropriate supply of public goods and services through an accountable process is prevented and cannot take root where it is most required. This should not be allowed to happen in Nepal. From the very start, the

third tier of government at the local level should be a pillar of strength for governance in the country.

Second, fiscal federalism is not just about the economic relationship between governments at different tiers that involves a process of resource mobilisation and allocation in meeting competing and multiple needs. It is also the space to resolve potential conflicts in the political, social and electoral arena in a democratic polity. While India has not paid sufficient attention to this broader aspect of fiscal

federalism because it has been lackadaisical in regards to the third tier of government, Nepal should proactively strengthen the foundation of a participatory democracy by capacitating the lowest tier of government adequately. It should evolve its own model of fiscal federalism that does justice to the needs and aspirations of its people. Such a model of fiscal federalism and broader relationships across the different tiers of government have to be founded on the recognition and use of hard and objective evidence from the grassroots.

DOING BUSINESS IN FEDERATED SRI LANKA: A CASE STUDY

Dr. PB Jayasundera, Senior Economist and Former Secretary, Srilanka

Sri Lanka adopted open market economy reforms in 1977 and incrementally implemented trade liberalisation, deregulation and privatisation of State Owned Enterprises with a view to create a private sector-led, market oriented development process in the country. However, a three-decade long conflict severely hampered the country's progress. Almost 10 years after the end of the conflict in 2009, Sri Lanka is confronted by several challenges to improving its competitiveness and private sector investment. Sustaining a high growth rate in GDP with an excess of 6 percent in line with the post conflict dividend, and public sector sponsored infrastructure development requires additional space for private sector investment and business activities. As the Central Bank Annual Report of 2016 explains, the prevailing weak investment climate is attributed to a range of factors including policy uncertainty, institutional weaknesses such as perceived level of corruption, weak regulations and infrastructure shortcomings. It has resulted in slow growth in domestic private sector investment, which has been around 25 percent of the GDP for many years, and which has foreign direct investments (FDI) of around 1 percent of the GDP compared to peer economies in the region. Factors such as macro-economic imbalances, legal and procedural impediments to investment, and lack of consistency in legal and judicial framework continue to pose challenges to the country's ability to benefit from a rapidly expanding Asian economic revival even after the end of the conflict.

The World Bank initiative to measure the business environment directs its attention towards regulations that either facilitate and accommodate business operations or simply hinder possible prospects. The Doing Business Index sets out to measure and quantify the degree of regulatory environments and to determine if they are conducive to business operations. Accordingly, economies are ranked by giving priority to 10 integral topics.

In Doing Business 2011 Sri Lanka's ranking was 102 out of 183 economies. Its performance in the stages of dealing with construction permits, registering property, paying of taxes and enforcing contracts was particularly weak as it ranks below 100 of the 183 economies considered and therefore pulled down the country's overall ranking. Recognising the importance of involving all stakeholders to improve the doing business environment, the central bank and government agencies initiated several actions to address each and every component relevant to the index measurement. Such actions included simplification of taxation, elimination of procedural steps involved in investment approval, dealing with construction permits and trading across borders. Court procedure was also looked into in order to devise a method to reduce the delay and improve the ranking in enforcement of contracts. The central bank also produced a booklet titled "A Step by Step Guide to Doing Business" which contains necessary information needed by an entrepreneur during each stage in the operation of business.

The country ranking improved to 99 out of 169 countries although progress remain sluggish in terms of registering property, getting credit, paying taxes and enforcing contracts. However, the rank fell to 107 out of 169 countries in 2015/16 owing to a change in policy regime in the backdrop of neighbouring country moving forward with reforms. The 2018 ranking of 111 out of 190 countries compared with its peers in South Asia is given in Table 1.

The Distance to Frontier score determines the absolute level of regulatory performance over time. It calculates the distance between each economy and frontier, which represents the best performance observed on each of the indicators across all economies in the Doing Business sample since 2005. An economy's distance to frontier is reflected on a scale from 0 to 100, where 0 represents the lowest performance and 100 represents the frontier. In the year 2017, Bhutan sits comfortably in the number

Table 1: Sri Lanka Doing Business 2018 ranking with peers in South Asia

World Bank Topics (Ranks)	Sri Lanka	Afghanistan	Bangladesh	Bhutan	India	Maldives	Nepal	Pakistan
Starting a business	77	107	131	88	156	68	109	142
Dealing with construction permits	76	185	130	82	181	54	157	141
Getting electricity	93	163	185	56	29	143	133	167
Registering property	157	186	185	56	154	174	84	170
Getting credit	122	105	159	77	29	133	90	105
Protecting minority investors	43	189	76	124	4	132	62	20
Paying taxes	158	176	152	17	119	118	146	172
Trading across borders	86	175	173	26	146	152	76	171
Enforcing contracts	165	181	189	25	164	106	153	156
Resolving insolvency	88	161	152	168	103	139	76	82
Overall Rank	111	183	177	75	100	136	105	147

Source: The World Bank

Table 2: DB 2018 Distance to Frontier (DTF)

Country	DB 2017	DB 2018
Sri Lanka	58.73	58.86
Afghanistan	37.99	36.19
Bangladesh	40.84	40.99
Bhutan	65.21	66.27
India	56.05	60.76
Maldives	53.78	54.42
Nepal	57.60	59.95
Pakistan	50.94	51.65

Source: The World Bank

one spot among the South Asian region while Sri Lanka follows behind to clinch the second spot. However, when comparing the recent data for the year 2018, Sri Lanka lagged behind Bhutan, India and Nepal respectively in view of the fast track reforms in India and Nepal.

The table below denotes statistics with regard to Sri Lanka and shows somewhat stagnant figures in the year 2018 in comparison to the year before resulting slowdown in reform process.

Table 3: Year on year statistics comparison

Sri Lanka	DB 2017	DB 2018
Starting a Business	87.52	87.74
Dealing with construction permits	69.31	69.33
Getting electricity	71.00	70.98
Registering property	45.92	45.92
Getting credit	40.00	40.00
Protecting minority investors	63.33	63.33
Paying taxes	53.46	53.70
Trading across borders	70.70	73.29
Enforcing contracts	39.31	39.31
Resolving insolvency	46.73	44.99

Source: The World Bank

The presence of excessive bureaucratic procedures in business activities, enforcement of contracts and property registration have placed the country at a significant disadvantage as a large public sector imposes higher compliance and transaction costs. Further high transaction costs associated with the dealing of a large number of ministries, organisations, regulatory agencies and regulations discourages the creation of new firms, limits growth of existing firms, encourages entrepreneurs to operate informally and paves the way for waste and corruption.

Sri Lanka has scored well in only starting businesses and trading across borders. Many obstacles have hampered the steady flow of trade in the form of high tariffs, para-tariffs and interference with agricultural activity. Moving forward

on the external trade front, the government has repealed the Exchange Control Act with the introduction of the Foreign Exchange Management Law of 2017 and the new Income Tax Law to be effective from 2018. Further, going beyond the existing Free Trade Agreement with India and Pakistan, the government has signed a Free Trade Agreement with Singapore. The government is also pursuing negotiations on an economic and technology cooperation agreement with India, and a Free Trade Agreement with China. Sri Lanka has also expressed an interest in pursuing trade agreements with Malaysia, Thailand and Indonesia with a view to improving economic links with ASEAN.

The figure below shows a comparison of countries including Sri Lanka with regard to difficulties that surface with trade.

Figure 1: Doing business indicators 2017

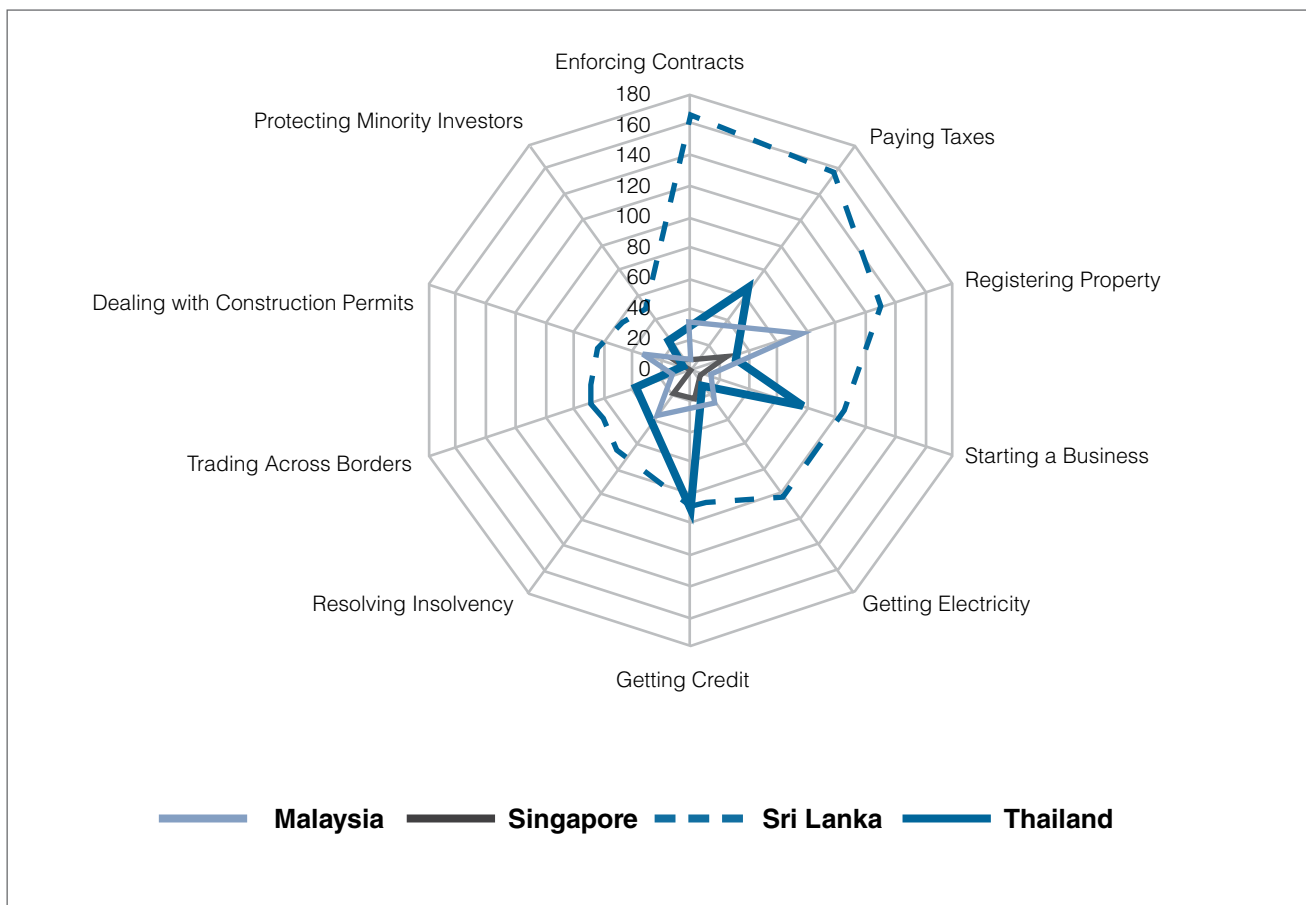
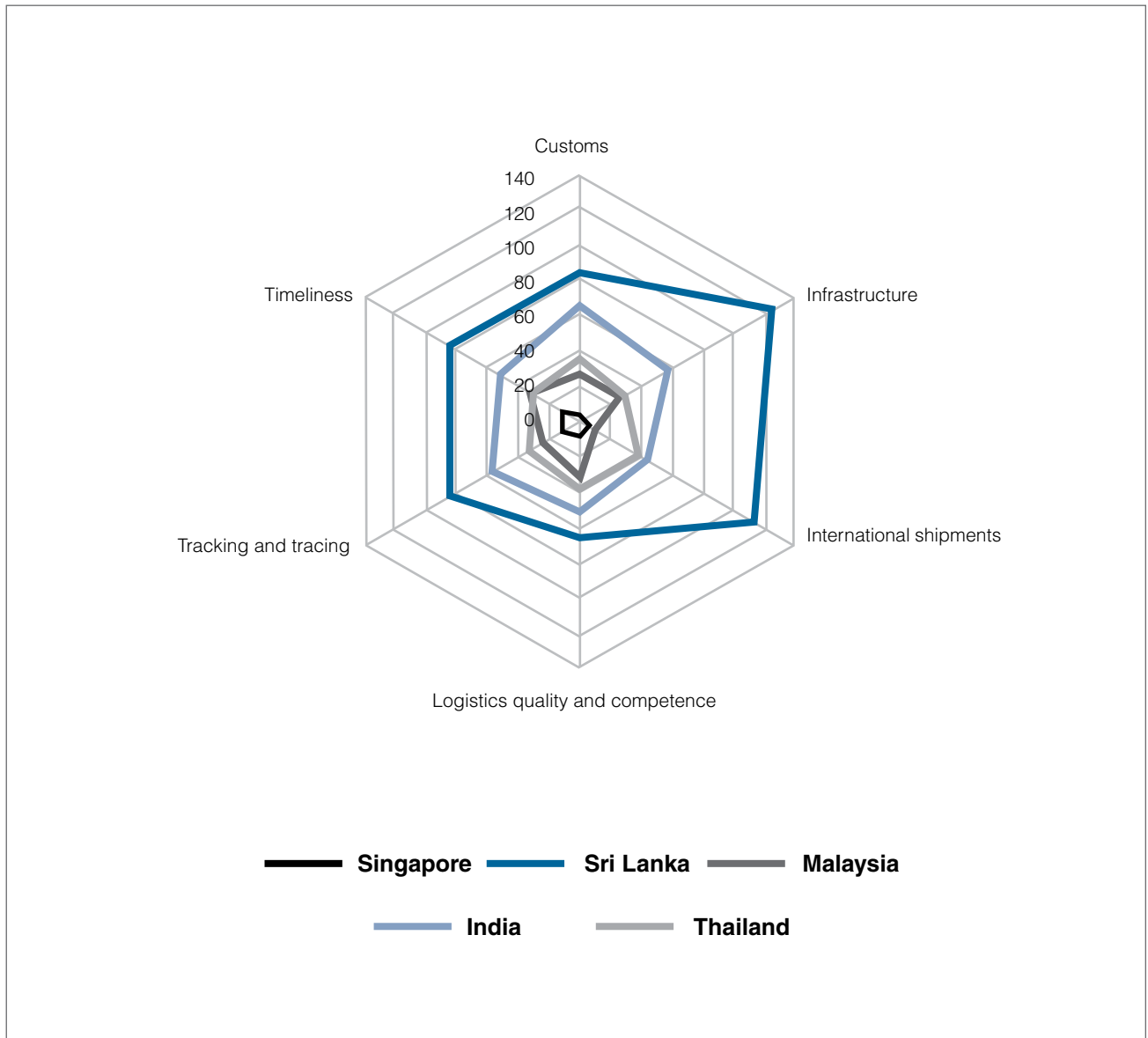


Figure 2: Doing business indicators 2017



In conclusion, whilst Sri Lanka has introduced several new initiatives to expand trade across borders, the improvement of doing business in Sri Lanka requires considerable changes in its public sector scale of operations. The reforms in a traditionally large public sector remain critical in terms of the scale of operation. Equally, reforms in overlapping

institutional and regulatory arrangements remain a major priority to get the Doing Business Index into a competitive position in the region, particularly in the context of its peers having accelerated reforms. However, such reforms remain challenging as several attempts in the past have not been successful and resistance continues.

FEDERALISM IN NEPAL: TOLERANCE, COMPROMISE AND LUCK

Jeffrey C. Fine, International Consultant, Canada

“Predictions are difficult, especially about the future”

-Yogi Berra (former New York Yankees baseball player)

This past year Canada celebrated the 150th anniversary of the passage of the British North America Act. This Act gave birth to the Dominion of Canada, an initial assemblage of four British colonies. Sensitive to the calamitous civil war south of the border that almost shattered the American republic, Canada’s “fathers of confederation” opted for a strong federal government. Today Canada is a very decentralised federation with ten provinces and three territories encompassing a land mass second in size to Russia. The provinces range from Prince Edward Island, with a population of 143,000 – equivalent to a smallish city – to Ontario, with 40% of the country’s 36.3 million inhabitants.

Over the past four decades, life has not been dull – there have been two referenda on independence called unilaterally by a separatist provincial (state) government in Quebec. In fact, the question of what constitutes a winning majority on separation (50% plus one? 60%?) was referred to the Supreme Court because there is no provision for “divorce” in our constitution, revised and “repatriated” amidst considerable acrimony only in 1982.

In crossing the Ottawa River from Ottawa to Gatineau, one is not simply traversing a provincial boundary. One is moving into a different jurisdiction with its own system of primary, secondary and higher education; its own code of civil law, its different arrangements for the delivery of health care and social services, and different levels of direct and indirect taxation levied and collected by the provincial government.

A national conference on education features the ten provincial Ministers of Education with the federal government as an observer.

In the midst of protracted renegotiation of the North American Free Trade Agreement (NAFTA) with the Trump Administration, we recently witnessed Alberta banning the import of wine from...the neighbouring province of British Columbia. Legal? Perhaps not, but the boundaries of provincial jurisdiction and the power of provinces more generally to create barriers to the movement of goods and services has yet to be tested. And both provincial governments are ruled by New Democrats, a mildly social democratic party. But provincial parties are quite distinct from their federal counterparts. And now the federal government is trying to reconcile their competing views concerning a new pipeline from the Alberta oil fields to the Pacific coast. British Columbia is opposed because of possible threats to its environment. Alberta sees the pipeline as vital to its future prosperity.

Is the Canadian federation at risk?

Not really since we have become inured to such squabbles and perhaps are even dangerously complacent about the ebb and flow of separatism in Quebec. We have gotten used to a Saskatchewan Party holding power by attacking “Ottawa” and other provinces.

We can never take the Canadian federation for granted. But over the years we have forged some important bonds that still hold us together. We recognise through tangible actions as well as in law our bilingual heritage and Quebec’s special culture, history and status. We have developed a nation wide system of health care that is run by each province but is based on the strongly held national belief that no one should be deprived of basic medical and hospital care because of an inability to pay for it. The provinces have worked out agreements

allowing students from one province to go to universities in the others. We have adopted – informally – a system for redistributing tax revenues amongst provinces to give substance to the principle that all Canadians, regardless of location should enjoy the same quality of basic public goods, including roads, schools, water and electricity.

At times we wonder about the time and effort required to reach agreement on what appears to be the simplest of issues.

Can we afford to be complacent?

Never. But we can be proud, not only of co-existing, but of building a society that actively tries to include citizens of very different origin, religious belief, culture and language.

So we welcome Nepal to the club of federations.

With tolerance and enlightened leadership, and a fair share of good luck, your future should be bright. But then again, as Yogi Berra wisely said, predictions about the future can be tricky.

NEW FEDERAL NEPAL- A GLIMPSE

Niraj Bahadur K.C., Nepal Economic Forum

With the completion of the general elections, Nepal has now embarked on a new phase to realize federalism.

Following are the five key points regarding the federal structure as mentioned in the constitution.

- ▶ **Federal Government:** The Federal Parliament will be comprised of two chambers, the House of Representatives and the National Assembly. Following the polls for Federal Parliament, 275 members will be elected to the House of Representative, with 165 members elected through the First-Past-the-Post (FPTP) system, and 110 elected through the Proportional Representation (PR) system.

The National Assembly will have 59 members, with 56 of the members elected by a committee consisting of the State Assembly, chairpersons and vice-chairpersons of the Village Bodies and Mayors and Deputy Mayors of the municipalities. The three remaining members will have to include at least one female and will be nominated by the President on the recommendation of the Government of Nepal (GoN).

- ▶ **Provincial/State Government:** The State Government will be elected via the provincial level polls and will be responsible for the governance of the concerned state. As per the constitution, each State Assembly will consist of a certain number of members. In this regard, the state members getting elected via the FPTP system is twice as many as the number of members elected to the House of Representative (via FPTP system) from the concerned state. Accordingly, 60% of the members will be elected via the FPTP system, whereas 40% will be elected via the PR system. For instance, in the case of Province 3, there are 33 constituencies, which means that 66 state members will be elected via the FPTP system, accounting for 60% of the total members. 44 state members elected via the PR system

will make up the remaining 40%. As a result, the State Assembly of Province 3 will have 110 state members in total.

Each province/state will have a Chief of State as appointed by the President of the Government of Nepal (GoN). The Chief of State will be the representative of the GoN. The State Assembly will also have a State Council of Ministers. This State Council of Ministers will be comprised of 20% of the total number of members of the State Assembly, including the Chief Minister.

- ▶ **Local Government:** Local level elections will elect the local executives consisting of the Village Executive or Municipal Executive. The Village Executive will consist of a Chairperson, Vice-Chairperson, Ward Chairperson, and other members who will be elected from each Ward. Likewise, the Municipal Executive will consist of a Mayor, Deputy Mayor, Ward Chairperson, and other members who will be elected from each Ward. As per the spirit of the constitution, local level elections in 753 local bodies have been successfully completed.
- ▶ **Revenue model:** The constitution provides authority to the government administrations at the federal, state and local level to impose taxes on matters falling within their respective jurisdiction. The taxes collected will then be distributed to the state and local level based on their expenditure and revenue capacity. Each state will then allocate the funds to their subordinate local levels based on their expenditure and revenue capacity.
- ▶ **Power structure:** The law endorsed by the Federal Government may be applicable to the entire nation and all the territory that falls within its borders. In contrast, the law endorsed by the state will be applicable to the

state alone. However, the Federal Government will have full authority to give necessary directions to any state on matters of national importance. Likewise, the GoN can give necessary directions to Local and Municipal Executives either directly or via the State Government.

With the completion of the federal and provincial elections, Nepal will begin a new political chapter guided by the notion of federalism. There seem to be multifaceted benefits of federalism. However, the primary concern in

regards to federalism has to do with the economic cost of the system. Put differently, under federalism, the ability of each state to thrive economically will be a major issue as they have to be self-sustainable. Likewise, the adequate and equitable distribution of resources to each state can prove to be a major challenge for the Central Government. Furthermore, in a country where vandalism and violence over a minor issue is routine, it will be interesting to analyze the required coordination among the Central, State and Local Governments.

POLITICAL RISK IN FEDERALISM: IMPLICATIONS FOR NEPAL'S ECONOMY

Samridhi Pant, Beed Management Private Limited

With frequent changes in the political regime, Nepal has always been at a high political risk. Federalism, which is an experiment that is yet to be tested in Nepal, also brings with it several political risks, some of which are briefly describe below.

Power sharing: As the modality for power sharing among federal units has not been properly defined, a puzzling situation could arise. As shown by the state of other countries under a federal system of governance, power sharing can be a major headache under a federal structure. Consequently, resulting power tussles could lead to problems of corruption, favouritism and nepotism, thereby impeding the prospect of doing business in Nepal.

Though a decentralized system of governance in Nepal is not entirely a novel idea, under federalism, power sharing can be even more of a challenge. Under this scenario, it would not be surprising to see a power struggle among the three levels of government in the forthcoming days. Power struggles could ultimately impact economic activities by creating major hurdles to doing business in federal Nepal. The constitution of Nepal currently calls for power sharing by the federal, state and local level governments in the following areas:

List of Concurrent Powers of Federation and State⁸⁵

1. Civil and criminal procedure, evidence and oaths (legal recognition, public acts and records, and judicial proceedings)
2. Supply, distribution, price control, quality and monitoring of essential goods and services
3. Preventive detention for reasons connected with the security of the country, prison and detention management, and maintenance of peace and order
4. Transfer of accused persons, detainees and prisoners from one state to another state
5. Laws relating to family affairs (marriage, transfer of property, divorce, persons on the verge of extinction, orphan, adoption, succession and joint family)

6. Acquisition, requisitioning of property and creation of right in property
7. Contracts, cooperatives, partnership and agency related matters
8. Matters relating to bankruptcy and insolvency
9. Drugs and pesticides
10. Planning, family planning and population management
11. Social security and employment, trade unions, settlement of industrial disputes, labour rights and disputes related matters
12. Legal profession, auditing, engineering, medicines, Ayurvedic medicines, veterinary, Amchi and other professions
13. State Boundary River, waterways, environment protection, biological diversity
14. Matters related to means of communication
15. Industries and mines and physical infrastructures
16. Casino, lottery
17. Early preparedness for, rescue, relief and rehabilitation from, natural and man-made calamities
18. Tourism, water supply and sanitation
19. Motion pictures, cinema halls and sports
20. Insurance business operation and management
21. Poverty alleviation and industrialization
22. Scientific research, science and technology and human resources development
23. Utilization of forests, mountains, forest conservation areas and waters stretching in inter-State form
24. Land policies and laws relating thereto
25. Employment and unemployment aid

List of Concurrent Powers of Federation, State and Local Level⁸⁶

1. Cooperatives
2. Education, health and newspapers
3. Health
4. Agriculture
5. Services such as electricity, water supply, irrigation
6. Service fee, charge, penalty and royalty from natural

resources, tourism fee

7. Forests, wildlife, birds, water uses, environment, ecology and biodiversity
8. Mines and minerals
9. Disaster management
10. Social security and poverty alleviation
11. Personal events, births, deaths, marriages and statistics
12. Archaeology, ancient monuments and museums
13. Landless squatters management
14. Royalty from natural resources
15. Motor vehicle permits

Ethnic federalism: Ethnic federalism defines the federal units on the basis of ethnicity. Ethnic federalism is a dangerous notion, as it can potentially be used as a political weapon to exacerbate ethnic conflicts at the subnational level. Ethnic cleansing is an extreme form of ethnic federalism, as witnessed in the case of the Amharas in Ethiopia and the Rohingya in Myanmar.

In economic terms, ethnic federalism restricts the movement of labour, capital and knowledge. Setting up a new business in other regional governments may be restricted. This can be seen in Ethiopia, where a person who wants to run a business or hold a government position in a particular region has to speak the local language. If not, they will be barred from holding that position.

Ethnicity in Nepal was a major issue while drafting the constitution in the recent years. Demarcating the federal units based on ethnicity and common identity was a major demand of various ethnic groups, including the Madhesi people from the Terai. With the completion of the federal and state level elections in the country, it will not be surprising to see states drafting policies along ethnic lines which can preclude the economic activities in the region.

Protectionism: Under federalism, provinces can protect their enterprises based on the rent seeking behaviour of local politicians. Such irrational behaviour of local politicians could result in endorsing substandard policies, thereby hindering the free movement of foreign capital. For instance, Canada faced a similar problem where persistent barriers to internal trade, regulatory differences, inconsistent standards, and restrictions on the free movement of goods and services placed Canadian firms at a disadvantage.⁸⁷

Nepal currently faces trade challenges as a result of its lower comparative advantage. Likewise, subsidies to protect national businesses is common in Nepal. In this case, provinces with a sizable number of industries may lobby the governing body to formulate policies to protect the enterprises. This could make doing business in federal Nepal particularly exasperating.

TRAVEL AND TOURISM IN FEDERAL NEPAL

Arya Awale, Beed Management Private Limited

Travel and tourism is a highly promising sector in Nepal; it creates jobs, drives exports and generates prosperity. In 2016, the total contribution of travel and tourism to Nepal's GDP was estimated to be NPR 177.9bn (USD 1.6bn) or 7.5% of GDP. This amount was expected to rise by 6.2% in 2017. Moreover, travel and tourism accounted for 945,000 jobs or 6.4% of total employment.⁸³

The adoption of federalism in Nepal has far-reaching consequences for all of the country's economic sectors, including travel and tourism. In Nepal's federal structure, power has been divided between three tiers of government—local, state and central—each of which has the autonomy to raise and spend revenue. 753 local bodies comprising of 6 metropolitan cities, 11 sub-metropolitan cities, 276 municipalities and 460 rural municipalities have been established along with seven states. All three tiers of government have the jurisdiction to collect revenue generated from tourism.

While on paper, Nepal's tourism policy is to, “accord priority to local people in the distribution of benefits of tourism industries” the recently tabled Natural Resources and Fiscal Commission Bill allocates 85% of taxes collected from activities such as mountaineering to the central government, leaving only 5% for local governments and 10% for state governments. This is a regression from the Local Self Governance Act 1999, which assigned 30% of revenue from mountaineering to local bodies. Commentators have noted that by reducing the capacity of local governments to generate revenue from tourism and natural resources, the bill represents a troubling move away from the decentralisation agenda.

The majority of Nepal's protected areas are significant tourist attractions. These areas generated NPR 552.7mn

(USD 5.36mn) in revenue in the fiscal year (FY) 2016/17, and are also under the purview of the central government. At present, the Department of National Park and Wildlife Conservation under the Ministry of Forests and Soil Conservation—a central government body—manages the revenue that is generated from 17 of Nepal's 20 protected areas. This includes revenue generated from entrance fees levied on tourists and fees levied on activities such as filming, helicopter landing, stone and sand mining, and wildlife activities. It is unclear whether any of these responsibilities will be conferred to the provincial or local levels under the federal structure.

Along with considerable challenges, federalism also presents opportunities for the travel and tourism sector. Under the unitary form of government, a central body, the Nepal Tourism Board, was responsible for promoting tourism in the whole country. The demarcation and establishment of seven distinct states presents an opportunity for states to run targeted tourism campaigns, highlighting the attractions of particular states, thereby driving the inflow of tourists. In this regard, Nepal could take a leaf out of India's book where many states have run very successful tourism campaigns over the years.

This could prove to be a particularly useful strategy for states that do not have many other sources of revenue such as State 6. State 6 could promote trekking and tourism in the Dolpa region by highlighting its pristine, untouched nature. The lack of physical infrastructure however will remain a key bottleneck for tourism in Nepal, particularly for the more remote states such as State 6 and 7. States will need highways, bridges and airfields in order for tourism to take off in the federal structure.

State	Tourist Attractions
State 1	Sagarmatha National Park
	Makalu Barun National Park
	Koshi Tappu Wildlife Reserve
	Kanchanjunga Conservation Area
	Namche Bazaar
	Gokyo Valley
	Taplejung
	Illam
State 2	Koshi Tappu Wildlife Reserve
	Parsa Wildlife Reserve
	Janaki Mandir
State 3	Parsa Wildlife Reserve
	Chitwan National Park
	Langtang National Park
	Shivapuri Nagarjun National Park
	Kathmandu Valley
	Kirtipur
State 4	Dhorpatan Hunting Reserve
	Annapurna Conservation Area
	Manaslu Conservation Area
	Pokhara
	Jomson
	Mukntinath
	Upper Mustang
	Manakamana
Bandipur	
State 5	Dhorpatan Hunting Reserve
	Bardiya National Park
	Banke National Park
	Krishnasar Conservation Area
	Lumbini
	Palpa
State 6	Rara National Park
	Shey Phoksundo National Park
	Dolpa Region
State 7	Khaptad National Park
	Shukla Phata Wildlife Reserve
	Apinappa Consersation Area
	Surmasorowar Lake
	Ugrathara Temple
	Nagarjuna Temple
	Ramarosharan Area

HOSPITALITY INDUSTRY IN FEDERAL NEPAL

Evleen Shakya, Beed Management Private Limited

With the successful completion of local, provincial (state) and federal elections in the country, many positive developments are expected in the hospitality sector in the coming days.

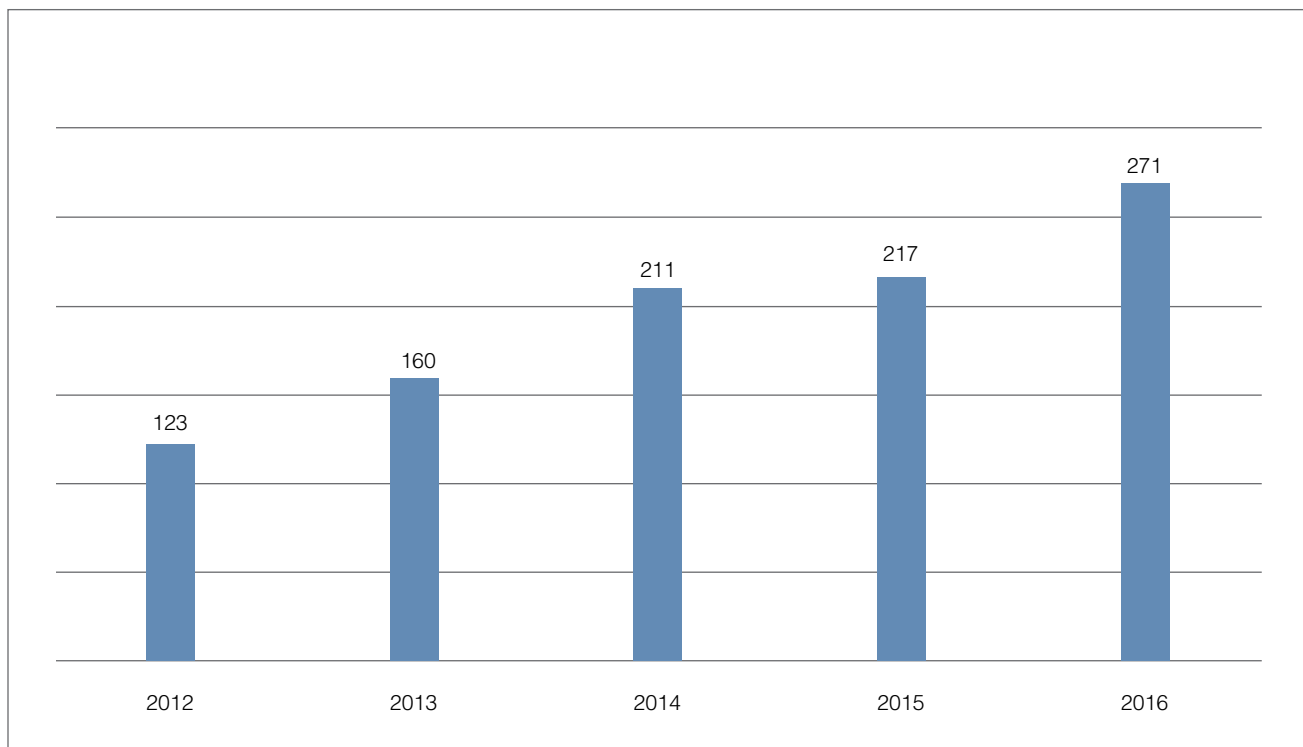
A look at the data on the status of hotels since 2012, has shown that the rising flux of tourists in the country has resulted in a substantial demand for hotels, as detailed below:

Year	Star Category Hotels		Non-star Hotels		Total Star and Non-Star Hotels	
	Total number of hotels	Total number of beds	Total number of hotels	Total number of beds	Total number of hotels	Total number of beds
2012	107	9371	746	22286	853	31657
2013	117	9506	909	25017	1026	34523
2014	118	9554	957	26625	1075	36179
2015	116	9710	960	27240	1076	36950
2016	120	10071	985	28171	1105	38242

Note: The time period is taken from January to December

Source: Department of Tourism, Nepal

Likewise, the number of homestays have increased by more than double since the year 2012.



Note: The total homestays figure includes both private and community homestays

Source: Department of Tourism, Nepal

With the increment in the number of tourists, many global hotels have been considering the Nepali market. A number of hotel chains including Aloft by Marriott Starwood, Doubletree Hilton by Hilton Hotels and Resorts, Sheraton by Marriott Starwood and Holiday Inn by Inter Continental Hotels Group have already signed management contracts with Nepali entrepreneurs.

Most of the good hotels in Nepal are clustered in Kathmandu, Chitwan and Pokhara. However, other highly potential tourism destinations lack good hotels mainly due to the absence of proper tourism infrastructure, transport facilities and road networks. As the country has achieved its political aspirations, nothing should now stand against the development of infrastructure. The provinces should focus on revamping their infrastructure by utilising allocated budgets and competing against each other.

Besides encouraging provinces to compete for the development of infrastructure and roads, the federal structure will also allow each province to highlight and promote their respective tourist destinations. For instance, with the federal structure in place, Province 6 is likely to promote the Dolpo region as a major tourist destination. Additionally, budgets are expected to be utilised accordingly for the development of tourism infrastructures and road networks. Apart from revamping infrastructure, the development of the hospitality sector will also depend on the policies endorsed by the new government in support of the promotion of the hospitality sector.

The advent of federalism in Nepal will bring about a plethora of positive changes in each of the provinces, ranging from the development of tourism infrastructures to the promotion of Foreign Direct Investments.

INFRASTRUCTURAL CHALLENGES AND REAL ESTATE MARKET UNDER THE FEDERAL STRUCTURE OF NEPAL

Raju Dhan Tuladhar, Beed Management Private Limited

The constant bickering among political parties and frequent changes in government has led to a weak system of governance which has proved detrimental to the development of infrastructure in terms of quality and timely execution of infrastructure projects. We often hear citizens complaining about the poor road conditions, poor water supply, poor electricity, poor communication system, poor drainage, poor waste management and so forth. Now, with the successful completion of the local, provincial (state) and federal elections, there is hope that new investments will be received to fuel infrastructure development projects, thereby leading to economic growth and improved standard of living.

Under the new federal structure, basic power for infrastructure development is provided to the federal, provincial and local governments. However, since most of the infrastructure projects are not confined to a particular locality or province, an issue of coordination among the three tiers of government is bound to arise. In this context, clear policies need to be drafted to demarcate the authority of each level of government, and committees that enable coordination among federal, provincial and local governments must be formed.

The allocation and distribution of adequate financial and natural resources among provinces will emerge as a key challenge under the new federal structure. Disputes related to sharing natural resources while developing infrastructure projects may arise. Such disputes may be similar to what occurred in India under the Kaveri River Water Dispute between the Karnataka and Tamil Nadu governments.

Hence, it is important that the National Financial and Natural Resources Commission as mentioned by the constitution is formed at the earliest.

Competition among provinces will be key to attracting the investment (domestic as well as foreign) that is so required for the development of infrastructure in each of the provinces. Though each of the provinces will be competing among each other by offering better investment schemes and facilities, safety and easy exit/repatriation of investment will be a salient factor in encouraging investment. Hence, it will be important that proper policies are drafted for safety as well as easy repatriation of investment.

Apart from investment in infrastructure projects, the new federal structure will further push growth opportunities for the real estate sector in each of the provinces. As such, decentralisation of the government will prompt demographic shuffling within provinces, thereby resulting in an increased demand of real estate. The new demand for housing may lead to land price speculation and increased investment in housing projects. In a nutshell, under the new federal structure, the price of land and housing may increase, however the increment could be at a diminishing rate within the Kathmandu Valley.

Besides land and housing, demand for building structures may increase as the concerned government needs to accommodate many of its ministries and departments, as well as quarters for bureaucrats. Thus as a result of increased demand for buildings, the price of construction materials might further escalate in the near future.

BANKING SECTOR UNDER NEW FEDERAL STRUCTURE AND ITS LIKELY IMPLICATIONS

Rojesh Bhakta Shrestha, Beed Management Private Limited

As Nepal has embarked on a new federal structure, the devolution of power across three layers of government is going to present both opportunities and challenges to the banking sector as well. The financial sector has been one of the most successful sectors following the liberalisation of our economy in the early 90's, and the new federal structure could further provide ample opportunities to enhance access to financial services across the country. However, the financial sector could also witness unnecessary pressure and challenges at the provincial (state) and local level.

Constitutional arrangement: The new constitution in Schedule 5 reserves central planning, the central bank, finance policies, banking, monetary policy, foreign grants, and aid and loans as federal powers. While, Schedule 6 outlines the operation of Banks and Financial Institutions (BFIs) in accordance with the policies of Nepal Rastra Bank (NRB), cooperative institutions, foreign grants and assistance will fall under the provincial powers with the consent of the Centre. Schedule 7 of the constitution defines the concurrent power of federal and provincial governments under which matters relating to cooperatives, insurance business operations and management fall. Moreover, as per schedule 8, cooperative institutions are under local level.

Changing role of the Central bank: With the changing landscape, the role and functions of the central bank i.e. Nepal Rastra Bank (NRB), is also going to evolve. The role of the NRB is going to be crucial as it will have to act as a banker and advisor to the provincial governments as well. Moreover, it will play a key role in facilitating the treasury operations and budget preparation of the provincial governments. The central bank will also have to make physical and operational arrangements to cater

to the specific needs of provincial governments and provincial stakeholders. Likewise, provincial NRB offices would have to carry out in-depth province specific research activities and monitor province level inflation to ensure that there are no fiscal disturbances that could disturb macroeconomic stability. Going forward, some form of supervisory activities can also begin from provincial offices provided there is a decentralisation of the operations of BFIs at the provincial level.

Access to finance: Even though the branch expansion of BFIs has seen a rapid growth over the years, these branches have increased largely in urban areas, due to which a majority of low income people from rural areas have been unserved. According to MAPFinscope Study, 2014, 61% of the population are financially served by both formal and informal entities, while 18% of the population does not have access to any financial services. Currently out of 753 local bodies across 7 provinces, there is a presence of a commercial bank branch in only 352 local bodies. Financial inclusion will have a positive impact in the days ahead as the government has made it mandatory to have at least one physical branch of BFIs in each local level body. Moreover, the central bank via the mid-year monetary policy has clearly mandated that banks must open branches in those local bodies that have minimum infrastructure availability within the end of the current fiscal year 2017/18.

Opportunities and challenges to the banking sector: As most BFIs portfolio are currently concentrated in urban centres, especially in Kathmandu, the new federal structure is likely to diversify bank portfolio and working areas across Nepal and provide new products and services. As this demographic shuffle is expected to bring a transitional economic boom, the lending towards transformative

enterprises, Public Private Partnership (PPP) projects, tourism sector, real estate and construction, and small hydropower projects is expected to increase in the days ahead. Likewise, in terms of services, banks will have an increased role in subnational government financing, treasury/revenue management and interstate transactions. Nonetheless, BFIs may face challenges such as human resource management, engagement with three layers of government, infrastructure development, stiff competition, and policy uncertainties amongst others in the new discourse.

Conclusion

Under the new constitutional arrangement, the new government has been formed, which marks an end of the political transition and provides a platform for a

stable government for the next five years. The primary objective of the new government will be economic transformation rather than political wrangling. The central bank and BFIs will have a significant part to play in the success of economic transformation, as the availability and access of capital is going to be a game changer in the new federal context. Due to the new structure, BFIs will have to now think from provincial and local perspectives rather than sticking with urban and Kathmandu-centric operations as the new structure provides a stable business and investment environment across Nepal. Moreover, due to the increased paid-up capital, BFIs are now in a more comfortable position to absorb and take risks, hence they should flex their arms and do business beyond the traditional and conservative way.

REVENUE ALLOCATION IN FEDERATED NEPAL

Shikshya Gyawali, Beed Management Private Limited

The constitution of Nepal 2015 provided the fiscal federalism model where responsibilities are shared among three tiers of government: central, provincial (state) and local. The allocation of the revenue as defined in the constitution are as follows:

local level is responsible for the collection of local taxes such as property tax, house rent tax, land revenue tax, business tax and vehicle tax. Whereas, the state and local level governments are responsible for the collection of entertainment tax, advertisement tax, registration charge

Sources of Revenue	Central	Province	Local
Excise Duty			
VAT			
Corporate Income Tax			
Individual Income Tax			
Payroll Tax			
Passport Fee/Visa Fee			
Entertainment Tax			
Advertisement Tax			
Registration Charge of Land and House			
Land Tax (Land Revenue)			
Property Tax			
Business Tax			
Vehicle Tax			
House Rent Tax			
Service Charge			
Punishment and Fine			
Tourism Charge			
Royalty from Natural Resources			

Source: Nepal's Fiscal Federalism Model in the New Constitution: Agenda for Amendments. Nepal Rastra Bank

The country's major source of tax revenue which includes custom duty, Value Added Tax (VAT), excise duty, corporate income tax and personal income tax comprises more than 80% of total tax revenue (refer to Figure 1). In the federal structure, all these major tax sources are assigned under the central government. The

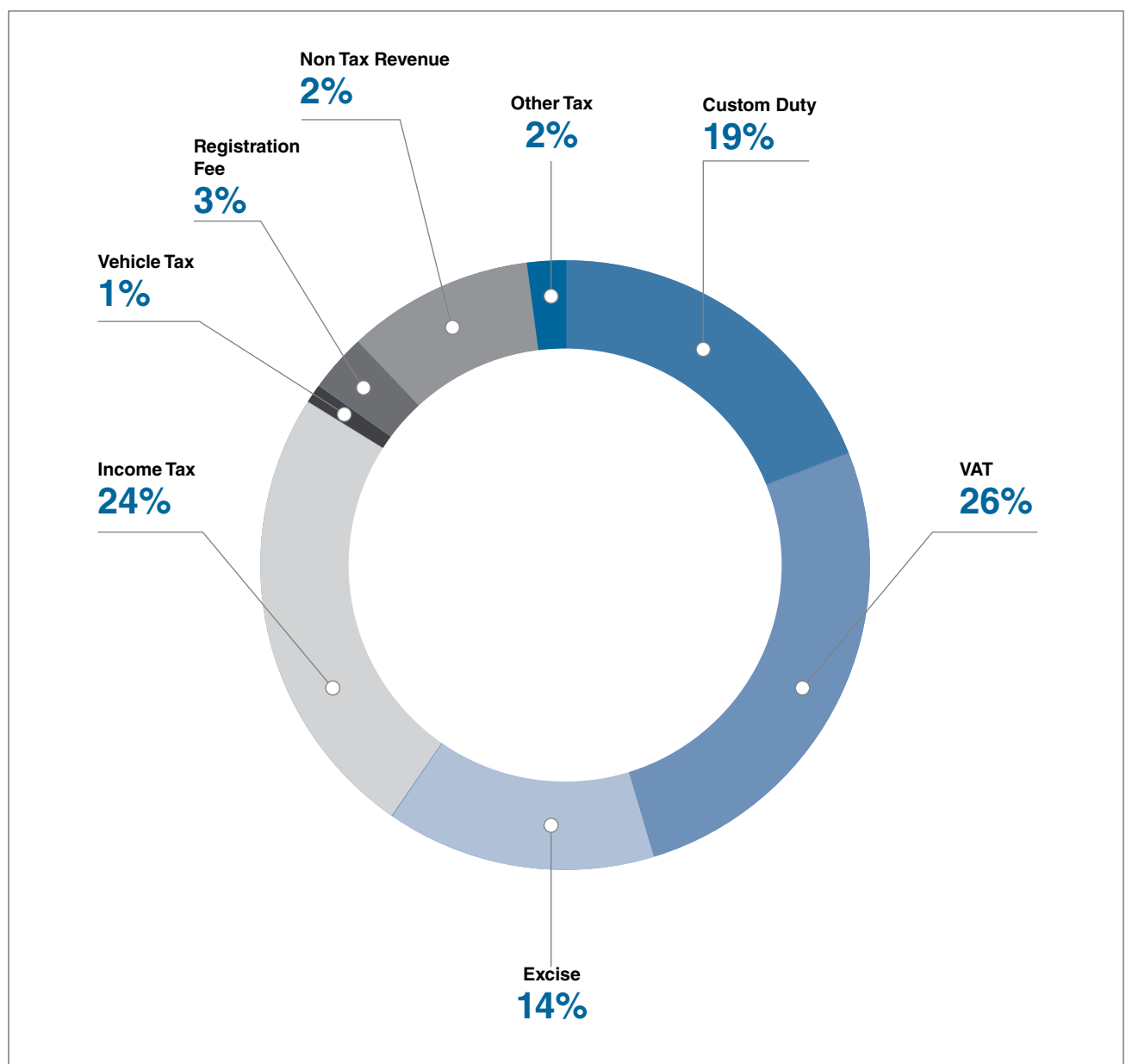
of land and house concurrently. Similarly, all three levels can collect certain service charge, royalty, tourism charge, and fines and penalty.

To put fiscal federalism into operation, three sets of acts have been introduced as mentioned in the table below:

S.N	Name of the act	Function
1	National Natural Resource and Fiscal Commission Act	The act enables the formation of revenues and royalties from federal consolidated fund among the three tiers of government in an equitable manner.
2	Local Governmental Operation Act	The act defines the functions of the various components of local bodies.
3	International Fiscal Management Act	The act guides to provide grant to subnational governments and distribute the proceeds generated from the use of natural resources among the three tiers of government.

Figure 1: Revenue Mobilization 2016/17

	In NPR Billion
Total Government revenue	607.17
Tax revenue	547.48
Non-tax revenue	61.69



Source: Nepal Rastra Bank, Current Macroeconomic and Financial Situation of Nepal, 2016/17

PROSPECT OF ALTERNATIVE ENERGY IN FEDERATED NEPAL

Sudip Bhaju, Beed Management Private Limited

Nepal has an immense dependence on hydroelectric power for its energy. This level of dependence led to the country being deprived of power for up to 16 hours in the dry seasons over the past few years. However, the days of massive load shedding seem to be over now as new hydropower plants have been connected to the national grid and the remaining gaps are being met through imports from India. But, the gaps in energy needs and sources of energy are still high, and considering the rapid urbanisation, these gaps are estimated to widen unless the big hydro-power projects come into full operation. This has led to a focus on developing the renewable energy sector⁸⁴ in Nepal, wherein solar and wind power is being seen as an important supplement to solve the energy crisis as the consumption of almost all fossil-derived fuels are imported in a refined form and the perpetual increase in petroleum imports has adversely impacted the existing fragile economy of the country.

The potential of the available renewable energy sources is huge in Nepal. For instance, installation of solar panels is becoming a common phenomenon, proving that solar energy is another viable and appropriate option for Nepal. Use of alternate renewable energy sources will also help reduce the dependency on traditional biomass energy resources and fossil fuels, manage the energy crisis of the nation and minimize the degradation of the environment.

Nepal has a varying topography from low plains to the high Himalayas, with scattered settlements that have sparse populations. These make it difficult for the citizens to access the different energy sources that are available. Currently, 40% of the population has access to electricity, and the rural electrification accounts for less than 29%, which means that much of Nepal is untouched by the national power grid, which proves as a deterrence of economic growth in these areas. In the absence of an adequate energy supply, these areas rely on traditional energy sources such as biomass – fuel woods, crop residues and animal dung – mainly for domestic usage as alternative energy sources.

These sources have negative environmental and health effects. Thus, the regional disparities in the availability of electricity in different states will need to be addressed through a rapid improvement in energy supply in these areas.

The demand for energy sources will be a constant, and it will have to be addressed under the federal and new political structure of Nepal, as micro-hydro and renewable energy technologies fall under the purview of local government. Local representatives will be answerable to the people, who will demand energy sources, as they currently do not have access to efficient service delivery of renewable energy and technologies. Such renewable energy sources require less resources and are less time consuming to set up compared to the big hydropower projects or grid extension. Energy is considered a key factor for the overall inclusive economic growth of the country.

Renewable energy development continues to be a high priority program of the government as it provides a cheaper solution for remote, sparsely populated areas that are unviable for grid extension, and as it is also clean, safe and environmentally friendly. The Government of Nepal's goal for the next 20 years is to increase the share of renewable energy from less than 1% to 10% of the total energy supply, and to increase the access to electricity from alternative energy sources from 10% to 30%.

Strong institutional frameworks and political will had limited the expansion and development of renewable energy technologies, despite the fact that they have high potential and are financially feasible. Local representatives will be pressured to be more accountable and will need to develop mechanisms that can create a conducive and enabling environment for the development of renewable energy in their concerned constituencies. It is critical to develop a strategy for sustainable, efficient energy usage for both hydro-electricity and renewable energy technologies. While developing the strategy, it is

important to move away from a blanket approach when it comes to understanding the resource endowments of the geography of the area to determine the most competitive format for harvesting renewable energy. It will be economically sensible only if the level of support and intervention is dependent on the technology type favourable for each location in order to make the best use of the locally available resources. A detailed feasibility and resource mapping study on the potentials of different renewable energy technologies across different regions can be the starting point in developing a pragmatic

renewable energy development plan. It will also be important to foster cooperation between stakeholder government agencies, private enterprises, non-profit organisations, and communities that are involved in the common pursuit of harnessing proven renewable energy technologies for sustainable development. It will be important to build local institutional capabilities to foster sustainable development assistance efforts; organise multidisciplinary teams and execute targeted technical assistance projects; and bring about successful adaptation and transfer of renewable energy technology.

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NEF PROFILE

Nepal Economic Forum (NEF) is a premier private-sector led economic policy and research organisation that seeks to re-define the economic development discourse in Nepal. Established in 2009 as a not-for-profit organisation under the beed (www.beed.com.np) umbrella, NEF is a thought center that is working to create positive transformations in policy reforms. One of the big updates for NEF this year was its feature in the list of Top Think Tanks in Southeast Asia and the Pacific in the 2017 Global Go To Think Tank Index. The report was released by the Think Tanks and Civil Societies Program under University of Pennsylvania. NEF stands out in being able to make significant strides to bring the private sector perspective and engage with both the public and private sectors in the development discourse. NEF is currently a recipient of the Open Society Foundations' Think Tank Fund.



NEF works in partnership with many Nepali and international institutions in its quest to mainstream the discourse on the Nepali economy, which has not been given the necessary space it deserves.

NEF has partnered with the Himalayan Consensus Institute (HCI) to facilitate the development of alternative development paradigms and successfully held the second Himalayan Consensus Summit 2017 in March 2017.

NEF BROADLY WORKS UNDER THREE AREAS:

BPRC

The Business Policy Research Center (BPRC) engages in research, dialogue and dissemination relating to pertinent economic policy issues. BPRC has been producing nefport, a quarterly economic analysis publication, nefsearch, a periodic research publication and conducting nefstalk, a platform for policy discourse.

PPCP

Through the Center for Public, Private and Community Partnerships (PPCP), the partnerships discourse is further elaborated through addition of the community dimension to existing models of public private partnerships. Apart from standalone interventions, the PPCP perspective is integrated in the work that NEF and beed initiate.



NEF operates in the domain of Development Consulting through its devCon division in conjunction with beed management.. It works with a variety of bilateral, multilateral, national and international NGOs in the areas of policy research, economic analysis, value chain analysis, enterprise development, sectoral studies and public private dialogue.

We are striving to ensure financial sustainability for NEF to complement the support it currently receives from beed management and the Open Society Foundations. If you are interested to support NEF, please do get in touch with sujeev.shakya@beed.com.np or niraj.kc@beed.com.np





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